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CAPITAL LOSS, CORRUPTION, AND THE ROLE OF WESTERN FINANCIAL INSTITUTIONS

HEARING

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

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CAPITAL LOSS, CORRUPTION, AND THE ROLE OF WESTERN FINANCIAL INSTITUTIONS

Tuesday, May 19, 2009

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to notice, at 10:06 a.m., in room 2128, Rayburn House Office Building, Hon. Barney Frank [chairman of the committee] presiding.

Members present: Representatives Frank, Waters, Maloney, Watt, Meeks, Moore of Kansas, Clay, Hinojosa, Baca, Lynch, Scott, Green, Cleaver, Ellison, Perlmutter, Carson, Kosmas, Himes, Maffei; Bachus, Castle, Manzullo, Biggert, Miller of California, Garrett, McCarthy of California, Posey, Jenkins, Paulsen, and Lance.

The CHAIRMAN. The hearing will come to order. The ranking Republican was required to attend a meeting of the Republican Conference. I can tell you from personal experience that when you have one of these jobs, you have to go to those things, as much as you might not like to, so he had no choice on this, and that's where he is, but he is on his way. I will begin with a brief opening statement, then I will call on my colleagues, and we will have an opening statement from the ranking member as soon as he arrives.

The question of corruption is a very serious one, and it is important as we go ahead with the inevitable global interaction economically that we do that as carefully and with as much attention to honesty as we would do domestically. And it's also the case that—I think it's very clear. Corruption internationally is not simply a matter of dealing with theft. That's important enough in itself but it clearly has a negative impact on our ability to accomplish the goal of improving the lives of people. That is, corruption is not just theft, it is theft from the poor, it is theft from the neediest.

So we address this not simply from the moral plane, which is, as I said, important in itself, but it is clear that if we do not do a better job of diminishing corruption, we hinder our ability to reduce poverty. Many of the gains that are posited as a result of the global interaction in the economy are diminished by the persistence of corruption. So this is a very important subject. This committee has jurisdiction over the Bank Secrecy Act and the Foreign Corrupt Practices Act, both of which are implicated here. And I believe this is an issue on which we may well be able to get some bipartisan support to move ahead.

And as I said—I say that because the ranking member years ago took the lead. I was one of those who joined in the lead that he and some others took to provide debt relief to the poorest countries in the world. But the good that you do by providing debt relief can be eroded if there is then a corruption with the funds that might be freed up by that. So we regard this as very much part of our mission to work to improve economic development to the world from the standpoint of improving the lives of people.

And I will now recognize the gentleman from Alabama.

Mr. BACHUS. I thank the chairman, and I thank you for convening this important hearing. It calls attention to a matter that is crucial in breaking the cycle of poverty in developing nations, and that is the role of corruption. Corruption is an unfortunate reality in all nations, but the consequences are particularly tragic in fragile developing nations, and also in many of those, corruption is widespread.

We have seen its effect in Nigeria where Dictator Abacha systematically looted the Nigerian treasury of literally billions of dollars during his tenure, leaving behind a desperately impoverished populace. We see it today in the Republic of Congo where the country's president and his family appear to be engaged in similar behavior, which will likely leave the same blanket of suffering. Simply put, corruption robs fragile nations, and more importantly its families, of a better future.

The humanitarian tolls of corruption cannot be denied. Chairman Frank mentioned some of them. We see the consequences in starving populations. We see it in nations ravaged by disease because they can't get adequate health care because money is diverted into the pockets of corrupt rulers and politicians. We see it in nations wholly reliant on the aid of other nations because of this corruption.

Yet the consequences aren't limited to these fragile developing nations or broken states, as they often are. Because fragile and what are referred to as broken states with a disenfranchised populace present a grave security threat to the United States. Afghanistan was a country that was a broken state. Corruption aggravates this situation.

There is also no doubt, as we have learned, if we didn't know it in the past, we have learned it in the last year or two, the interconnectivity of our economies. The United States and other nations who trade with these countries benefit from their economic expansion and their growth. We all benefit from economic growth across the globe. And many of these countries represent a global consumer base for our exports and for imports. It's a win-win situation when we trade goods and services. And corruption robs us of this economic growth which benefits all of us.

So corruption is something that affects all of us, no matter where it occurs. Corruption in the developing world also impacts the global banking sector. The global banking system still can easily be exploited by those seeking to conceal or laundry the proceeds of political corruption. A concerted international effort involving close cooperation between regulators, law enforcement authorities, and financial institutions is absolutely essential to preventing further exploitation.

I would like to recognize Chairwoman Waters. She is not here, but her efforts on that front have been extraordinary. She has long pointed out that in developing nations, corruption often isn't limited to the ruler, but involves his or her family and their associates. And she has fought for years to make sure that U.S. and international law enforcement focus on these politically connected people in such regimes, to make certain that when they do loot these nations, as much money as possible is recovered and goes back to where it rightfully belongs.

Mr. Chairman, I appreciate your efforts in this regard. I would like to close just by saying we have invited Mr. Jack Blum to appear before the committee. He's a world renowned expert on issues such as I have spoken about and what policy steps we can take, and he has worked on them extensively in a number of different capacities and testified on this matter, I remember in 2002 on a hearing I chaired about recouping stolen sovereignty assets. So, I thank you for your efforts.

The CHAIRMAN. I thank the gentleman. Let me just say, I appreciate the fact that he mentioned our colleague, Ms. Waters. She has played the role, he said, and in fact, it was on the return of a congressional delegation of this committee from Africa, a bipartisan delegation, in which having listened to people, including nongovernmental organizations as well as officials and members of Parliament in four African countries, that she said, we have to get into this. We heard that. And it takes a while, because we have had a fairly busy agenda, as people know. But this hearing is a direct result of that congressional delegation. The gentleman from North Carolina was on it, and we clearly learned then the importance of this for development efforts. So we're very pleased to be able to do this.

And now I will recognize the gentleman from Georgia, Mr. Scott.

Mr. SCOTT. Thank you, Mr. Chairman, and I certainly appreciate this hearing. It couldn't be more timely, and I certainly concur with you and what your words were, because nowhere is this issue of corruption more prevalent than on the continent of Africa, and it's most important, vitally important that this Congress put Africa at the front and center to make sure that our monies that are going there are going for the right purposes.

I just returned from Africa about 3 weeks ago, went into the Congo and saw firsthand what is happening in the Congo. In Fasio, the same thing, which is the poorest countries in the world on the continent of Africa, but yet the richest countries in the world are on the continent of Africa. The dynamic of this situation is here is a continent and countries that are full of the natural resources, the minerals, the diamonds, the gold, the oil, the rubber, all of these, for centuries they have been exploited by European powers, the colonialization. The remnants of this exploitation still remains in the presence of these dictators and heads of these regimes. Now here we come with our funds. We have to make sure that they are not being misused in corruption.

When we got back the very next day, Secretary Clinton came before our Foreign Affairs Committee and I got to ask her that question as well. She was very passionate about it, and I am so pleased to see this committee moving forward, and the Foreign Affairs

Committee moving forward, and the Secretary of State moving forward to say that we do not need our taxpayers' dollars going to prop up these regimes in Africa that are bleeding the countries of their natural resources, and with the wretched conditions of poverty unlike any you have seen on the face of the Earth.

There's no greater example than what is happening in the Congo. For example, the president of Congo's son's credit cards could be traced back to a bank account in Hong Kong that received the proceeds from Congo's oil revenues. For just 1 month, his credit card bill was $32,000. And that money could have paid for 80,000 Congolese babies to be vaccinated against measles, which is a leading cause of child death in that country.

The question has to be, are our taxpayers' dollars propping up these banks, and also helping to prop up the ease of corruption in these developing countries around the world, and especially in Africa? There are indeed existing international standards, but the question has to be, are these financial institutions truly paying attention to them or taking them seriously at all? And as billions of dollars in developing countries being transferred to Western financial shelters in a matter of a year, this is cause for real concern.

So ensuring prudent management of resources, promoting accountability and openness is of utmost importance, as is allowing for vital information to be put in the hands of civil society groups and therefore its citizens. Too often the common citizen is left out while their country engages in fraudulent activities with regards to their own natural resources, as I mentioned. And with many conflicts, the results of a country's extractive industries, we must also look into the corruption behind a country's extractive industries, because without a strong stance on these corrupt officials, this will only lead to poverty increases, social investments being put by the wayside, and funds continuously being misappropriated and misused.

And finally, greater accountability for the large revenues coming from these industries, working to generate economic growth from these revenues and reducing poverty are all aspects we should focus on. However, without reform in transactions being made between these developing countries and Western financial institutions, it will be harder and harder to move forward.

Chairman Frank, I can't thank you enough personally for your leadership in moving on this vital issue and on behalf of those suffering millions of people in Africa, I want to say thank you for providing leadership on this important issue.

The CHAIRMAN. I thank the gentleman. Our colleague from Texas had a statement but he had to go off and make a quorum somewhere, so we are now going to begin. I will reiterate that we have the entire legislative jurisdiction in this committee and it is our intention to move legislation. So I thank the witnesses. You are helping us with a process that we think is going to result in better laws. We will begin with Mr. Raymond Baker, who is the director of Global Financial Integrity, an impressive title.

STATEMENT OF RAYMOND W. BAKER, DIRECTOR, GLOBAL FINANCIAL INTEGRITY

Mr. BAKER. Thank you, Mr. Chairman, Ranking Member Bachus, and members of the committee. I appreciate the opportunity to appear before you today.

There is no evidence that the dollar volume of corrupt money flowing across borders is declining. On the contrary, it appears that corruption may be at the highest levels ever, particularly with very large sums of money shifting out of China and Russia, while flows likewise continue out of Africa, Latin America, the Middle East, Asia, and states of the former Soviet Union, and indeed out of Western countries as well.

How can this be? To answer this, we must place the issue of corruption into its larger context—the global shadow financial system and its attendant culture of opacity. Since the 1960's, we in the Western world have created and expanded an entire integrated global financial structure to facilitate the movement of illicit money across borders. This structure now comprises a number of elements: Tax havens; secrecy jurisdictions; disguised corporations; anonymous trust accounts; and fake foundations. Falsified pricing in import and export transactions is by far the most frequently used element in this structure. Money laundering techniques are widespread, and there are holes left in the laws of Western nations which serve to facilitate the movement of money through the shadow financial system and into our own economies.

Regarding this last point, for example, in the United States, it remains legal to bring into this country proceeds generated abroad from handling stolen property, counterfeiting, contraband, slave trading, alien smuggling, trafficking in women, environmental crimes, virtually all forms of tax-evading money, and more. Having initiated the anti-corruption effort in 1977, we are now far behind our European counterparts in the range of illicit monies that we bar from entering our country.

This global shadow financial system moves cumulatively trillions of dollars of illicit money across borders. It equally facilitates the shift of the proceeds of corruption by foreign government officials, criminal activities such as drug trading and racketeering, terrorist financing and tax evasion.

Global Financial Integrity has recently completed an analysis of illicit financial flows out of developing countries, utilizing well-accepted economic models. We show that somewhere between $850 billion to more than $1 trillion a year of illicit money flows out of developing countries on an annual basis. This massive shift of illicit money abroad is the most damaging economic condition hurting the global poor. It drains hard currency reserves, heightens inflation, reduces tax collection, worsens income gaps, cancels investment, hurts competition, and undermines trade. Quite simply, it contributes in a major way to the environment in which corruption thrives.

Now, how can we address these problems? Three measures can substantially curtail the cross-border flow of all forms of illicit money:

First, financial institutions around the world should be required to know the beneficial owners of entities with which they do business.

Second, it is time to institute automatic exchange of key elements of information across borders, including for non-citizens their earnings on accounts. Such automatic exchange of information exists today between the United States and Canada and within the European Union via the EU Savings Tax Directive.

Third, country-by-country reporting of sales, profits, and taxes paid by multinational corporations would do more to curtail the shadow financial system and the culture of opacity than any other step.

To address the flow of corrupt money per se, three additional steps are recommended:

First, we should harmonize predicate offenses under the anti-money laundering laws of all countries cooperating with the Financial Action Task Force.

Second, strengthened know-your-customer regulations as they apply to foreign account holders should be implemented. Adding a specific point on suspicious activity reports for corruption is needed.

Third, lists of politically exposed persons, PEPs, should be available for all countries receiving development assistance, and the use of PEP lists should be required by financial institutions.

The fight against global corruption is not being won. As we did in our early passage of the Foreign Corrupt Practices Act, it is time once again for strong U.S. leadership.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Baker can be found on page 44 of the appendix.]

The CHAIRMAN. Thank you, Mr. Baker.

Next we have Ms. Anthea Lawson, who is the lead investigator of financial institutions at Global Witness.

STATEMENT OF ANTHEA LAWSON, LEAD INVESTIGATOR, GLOBAL WITNESS

Ms. LAWSON. Mr. Chairman, members of the committee, thank you. Global Witness is a nongovernmental organization that investigates the links between natural resource extraction, conflict, and corruption.

The world's poorest countries would be far less poor if revenue from natural resources that should be spent on development had not been looted by their senior government officials. Banks are not permitted to accept corrupt funds under existing international standards, but too often they do not seem to be taking this obligation seriously.

I will present three examples from the latest Global Witness report, "Undue Diligence: How banks do business with corrupt regimes." First, we show that the international regulatory regime governing banks has not put into place effective procedures to prevent them handling the proceeds of corruption, as have been used to stop the handling of terrorist funds.

Dennis Christel Sassou-Nguesso is the son of the president of Republic of Congo, which earns about $3 billion a year from its oil,

but where a third of the population don't live past the age of 40. Between 2004 and 2006, he spent hundreds of thousands of dollars on luxury clothes and shoes with money that derived from Congo's oil sales, as Representative Scott has reminded us. Using a Caribbean tax haven, Anguilla, he set up a shell company, disguised his ownership of it, and opened a bank account in its name at the bank in Hong Kong. Money deriving from Congo's oil sales was paid into this account.

When the credit card bills came in each month after the designer shopping sprees, the Anguillan company services provider that was fronting for him wrote to the bank instructing payment of the bills from this account. He is named on these payment instructions as the owner of the credit card, and these payment instructions were stamped, presumably by the bank, "record of terrorists checked." This is a fascinating insight. The bank ran his name through the terrorist watch list to make sure that he's not a terrorist, but does not appear to have checked whether he's a political figure and whether there's a high risk of corruption.

The U.S.-led campaign to create international controls against the financing of terrorism has had results. Banks are now checking that their customers are not terrorists. But there has been no similar campaign to ensure that banks worldwide do not accept the proceeds of corruption.

In our second example, the United States took action against a bank for doing business with a corrupt regime, and then a bank in Europe continued to do business with a member of this regime and handle its funds. In 2004 to 2005, Riggs, as you know, was finished off after holding accounts for President Obiang of Equatorial Guinea and his corrupt government. More than 3 years later, the British bank, Barclays, was still holding an account for Teodorin Obiang, the president's son, at a branch in Paris. Teodorin reportedly earns a salary of $4,000 a month as a minister in his father's government, yet he owns a $38 million mansion in Malibu, California, and a fleet of fast cars.

Global Witness has asked Barclays what due diligence it could possibly have done to reassure itself that the source of funds in this account is not corrupt, and they can't tell us. This case illustrates the need for the United States to take further action internationally to ensure that all the major banking centers are operating at the same level.

Without further steps, not only will the fight against corruption be ineffective, but U.S. banks will not be operating on a level playing field.

Our final example reviews Citibank's facilitation of banking activities that allowed Charles Taylor, the ex-President of Liberia, now on trial for war crimes, corruptly to divert timber revenues to his personal use during the conflict there. His regime instructed one of Liberia's main timber exports to make its payments in lieu of tax directly into a number of nongovernmental bank accounts, including Taylor's personal account at a Liberian bank. These dollar payments could not have taken place without the correspondent relationship between the Liberian bank and Citibank in New York, through which the payments were routed, which gave Taylor the

means to receive these corrupt timber revenues into his own account.

Banks must be forced by regulators to improve their due diligence practices. Banks must not accept funds unless they can identify the beneficial owner and they can demonstrate strong evidence that the funds are not corrupt.

The United States has been a driving force behind the Financial Action Task Force, or FATF, the intergovernmental body that sets the global anti-money laundering standards and measures member states' compliance with them. The United States should use its influence to ensure that FATF undertakes further steps to make anti-corruption rules and on money laundering more stringent, and names and shames countries that are not compliant with FATF standards or that are not enforcing them, so that those countries that are ahead of the curve are not penalized. We would be pleased to see this committee take up these issues, and I would be happy to answer any questions.

[The prepared statement of Ms. Lawson can be found on page 94 of the appendix.]

The CHAIRMAN. We have been joined by our colleague, Ms. Waters, and I did want to tell her, let me say it publicly, that both the ranking member and I acknowledge the very important leading role she has taken in bringing this subject forward.

Next we have Mr. Nuhu Ribadu, who is the former executive chairman of the Economic and Financial Crimes Commission of the Government of Nigeria.

STATEMENT OF NUHU RIBADU, FORMER EXECUTIVE CHAIRMAN, ECONOMIC AND FINANCIAL CRIMES COMMISSION (EFCC) OF NIGERIA

Mr. RIBADU. Thank you, Mr. Chairman, Ranking Member Bachus, and members of the committee. Let me thank you for the honor of this invitation. As you said, my name is Nuhu Ribadu, and I am the former chairman of the Economic and Financial Crimes Commission of Nigeria, assigned with the responsibility of fighting economic crimes in Nigeria that came as a result of pressure from the international community, FATF, the U.S. Government, and the U.K.

I have heard a lot, and you have said eloquently on the issue of how terrible corruption is, the damage it is doing to us, not just Africa, but the world. But I also want to tell you from the side, from those who are at the receiving end, and I'm one, I'm sitting here, an African, a Nigerian, a picture of really what really happened to us as people who have been reduced to a level of more or less living on the kindness of others, our honor, our dignity, our respect, everything has been destroyed. We are today at the bottom of the ladder in the world, and that is not fair.

And that is what I want to share with you. You have said everything, but I want to give you a little bit of statistics of what really is happening, what has happened to us as people. AU, for example, the African Union, came up with a figure that as much as $140 billion is wasted, going to corruption, stolen from the people of Africa, the poorest people of the world; $20 billion annually goes out of the country, stolen. I want to talk about money coming from companies

that are doing business. This is stolen money going out of the poorest country. Imagine what that money can do. This is far, far more than the entire support that comes from United States to the continent.

The U.K. Commission that was set up by Tony Blair came up with the figure that as much as $93 billion is out there in the financial institutions of the West coming from Africa, stolen. Nigeria is a country, a country that I come from, and as much as about $440 billion in 3 decades from selling of crude oil, all wasted, stolen, nothing to show for it. This is money that is probably 6 times what was needed to change Europe after the second World War. Today go to Nigeria and see, you will realize what we are talking about, the crime of corruption. It's very unfair. It's tragic.

But I'm here to also tell you my own experience. I fought corruption in Nigeria. I have seen at close range what is happening to us. I have also, as a person who more or less is responsible for bringing out the case of Halliburton, the one where Halliburton gave about $184 million as a bribe to Nigeria. Where Halliburton today is punished in the United States by probably as much of a fine of about $600 million. But Halliburton still is getting away with $6 billion of contracts, and there are people out there in Nigeria who have received this money, and they are continuing to continue doing business as usual. The same thing, for example, with Siemens. The same thing with all the other companies. Siemens is a company that was punished by the U.S. Government. Today Siemens is doing the same business in Nigeria.

Mr. Chairman, this is what is happening to us. I fought corruption. I know what it has done to us. The problem, for example, of Nigeria, while we are attempting to address it, I know it is as a result of corruption that we have this situation where we found ourselves. I brought one governor who was in charge of one of the states in the Niger delta. He gave me $15 million cash in a box to stop me from prosecuting him. I refused this money. I took him to court and I charged him and I handed that money also as evidence in Nigerian court. Today, that gentleman is probably one of the most powerful individuals in our country. He's one of the most powerful people in charge of the ruling party.

It is happening. It has done damage to us growing, people like us, who are desperate for change, who are fed up, who don't want this type of thing that they have done to us. The leaders from Angola to Zimbabwe, those who are in charge of our own affairs, have done this damage to us. That is the reason why, Mr. Chairman, we think that we need help. While sitting down out there, before getting into this hall, I read your Declaration of Independence, the one that you did hundreds of years ago. I saw where you, the Congress, dreamt and wanted freedom, liberty, and the pursuit of happiness. We are equally entitled to that. We want that, and we desperately want the world to come in and support us.

Those of us who are victims of this corruption are helpless, are powerless. Today I have been kicked out of Nigeria. I can't even go there. I survived an assassination attempt. Because some of us few who had the courage to stand up and say enough is enough, let's stop this, let's move forward, today, Mr. Chairman, this is what—it is still coming down to the fact that we must do it ourselves. No-

body else will do it. It is we, the Africans, and I can assure you, people are fed up. People are tired. But we need the good people of this world. We need you to support, to stand by us and see that it is possible for us to also have a change, change that is taking place in the world today. We have seen those who, not necessarily even one deserved a change, but they are getting it. But we in Africa are desperate for change.

Thank you very much, Mr. Chairman. I will wait for your questions.

[The prepared statement of Mr. Ribadu can be found on page 115 of the appendix.]

The CHAIRMAN. Thank you.

Ms. Monica Macovei, who was formerly the minister of justice in the country of Romania.

Ms. Macovei?

STATEMENT OF MONICA MACOVEI, FORMER MINISTER OF JUSTICE, GOVERNMENT OF ROMANIA

Ms. MACOVEI. Thank you, Mr. Chairman, ladies and gentlemen. I was the minister of justice in Romania in 2005–2006. I was fired in April 2007, 3 months after Romania's accession into the European Union. It's not about my situation I want to talk, it's about my experience as a minister of justice fighting corruption.

At the beginning of my mandate, I had to establish the strategy and the action plan to fight corruption under a safeguard closed by the European Union in Brussels, and before I established the benchmarks and the concrete activities and measures, each institution within the anti-corruption area had to do. So there were benchmarks in high-risk corruption areas such as public procurement, privatization, transparency of public spending, in particular all the contracts from the state money, anti-money laundering legislation, independent and efficient law enforcement agencies, conflict of interest incompatibilities, funding political parties and campaigns. And then we started after we made these benchmarks, we started the implementation.

Now I took it seriously, and the same did the anti-corruption prosecutors office, which I set up in 2005, and these prosecutors started to investigate politicians from all the parties, including the parties in power, and high officials. This was really a premiere in Romania. I think in the last 2 or 3 years, this prosecutors office prosecuted, sent to trial about 20 current and former members of the parliament and of the government for corruption and fraud and other officials from all areas, including from the judiciary.

The reaction to this prosecution came in particular with priority from the political class. And I saw the behavior of my colleagues in the government when people from the parties in power started to be investigated and prosecuted. It was unbelievable. We are in power and we are investigated. So consequences of this continuous public pressure, I would say political pressure for those investigated, all claiming that these are political cases, although they are, as I said, coming from all the political parties. Then attempts from the parliament to change the procedural law such as to try to avoid being investigated.

And I can give you a quick example. We had—and also an example of the level of bribe, which shows it better. We had in 2007 a minister of agriculture taking a very low-level bribe in terms of money, about 15,000 euros, and also sausages and other products for—allegedly for giving contracts about 6 million euros to some private companies. And also speaking about the level of bribe, we heard the cases with members of the judiciary who were prosecuted and convicted for amounts around 100, 200 euros, which shows to me not that their bribe is small, but it shows a practice.

So coming back to the reaction of the politicians, when such cases became public, and of course they were damning the use of surveillance measures, interceptions, and filming. One measure taken by the parliament without any public debate was to make this procedure impossible. For instance, one provision was saying that a person cannot be intercepted before—unless he's informed that an investigation is going on against the person, so therefore making all these surveillance measures useless.

These provisions were not passed, because they were rejected and they were sent back for examination by the president of the country, but they showed the attitude of the politicians when they are, of the majority of the politicians, when they are under investigation. They try to use any means, and they have the decision in their hands, and they use it to fight back.

Another example of political behavior is the decision to lift immunity when the prosecutors ask for the parliament. These cases, many of them were rejected, were denied, and then they were reheard again. These cases took about between 5 months and over 1 year for each case to be decided in a way yes or no, and those many MPs said that they have to look at the evidence, so they basically tried to take the role of the charge. So all these together shows an opposition to this investigation. Basically, what they are trying to do is invoking civil rights in all these changes basically to establish and practice the right not to be investigated.

I was supported by the president of the country. When I was a minister, I was independent. I didn't belong to any political party. This is how it happened. As I said, I had the support of the president of one party which supported me. After the accession when all the politicians saw that—achieved the objective of being into the European Union, the party which supported me was asked to withdraw the political support for the minister of justice. It refused and then it was basically excluded from the government.

There are sustainable things and things which could not be changed back, as, for instance, this anti-corruption prosecutor office, which is still there, and which is still investigating, including politicians and which is still under attack, but I think the most important thing is that these people are doing their job. Thank you.

[The prepared statement of Ms. Macovei can be found on page 112 of the appendix.]

The CHAIRMAN. And next, Mr. Jack Blum, who was the former head of the UN Experts Group on Asset Recovery and has a very extensive background in dealing with this. And I said that this is going to be a bipartisan issue. We have witnesses, and the practice is that most witnesses are proposed by the majority. The minority gets to propose witnesses. I must say here I think the choices were

totally interchangeable. Mr. Blum—sometimes there are differences on issues, but this is case where I think just the very selection of witnesses shows that there's a great degree of consensus.

Mr. Blum?

STATEMENT OF JACK A. BLUM, ESQ., FORMER HEAD, UN EXPERTS GROUP ON ASSET RECOVERY

Mr. BLUM. Mr. Chairman, it's a pleasure to be here this morning, and I thank you and the ranking member for their kind remarks. This committee did quite admirable work 7 years ago in putting together a hearing to discuss these issues. Unfortunately, the events of the last number of years made it very difficult to continue down that path.

I am currently involved in the Nigerian Halliburton bribe case, representing the government of Nigeria, trying to get mutual legal assistance from the United States. Now that case and other cases illustrate the complexity of the problems we're dealing with, and they really are complicated problems.

The screaming frustration of people looking at something like the family of the Obiangs running Equatorial Guinea where you have 700,000 people in desperate poverty and a per capita GDP that makes it 8th highest in the world, is unbelievable. Yet there's nothing, it seems, anyone can do about the fact the Obiangs are running the country and stealing it blind, other than to wait for them to either depart office and try to prosecute after the fact, or wait for some form of criminal complaint or conviction to come forward, and then begin a process of searching for the money.

But failing to have that criminal process undertaken, either in Equatorial Guinea or against a company that's actually taking the oil out of Equatorial Guinea, everything is absolutely okay. And if a bank gets a deposit from the Obiang family, the simple solution for the bank is to file an SAR, report to the government that in fact there has been a suspicious transaction, and then it's really up to the bank as to what they want to do in terms of handling the money. And, of course, the situation is, and this is very clear, that if a U.S. bank doesn't take the money, somebody will take the money and then funnel it into a U.S. bank through some other shell, either a trust or a shell company or whatever.

This business of sovereignty protects a lot of sitting crooks. And I'll give you another example. The government of Kazakhstan, which is notorious in its corruption, yet because the same people are running the government, there are no charges and no basis for anybody going after their assets or even saying we can't do business with them. This is a very frustrating problem, and there are no simple solutions to it.

The idea of national prosecution such as we have in the Foreign Corrupt Practices Act is a very appropriate approach. It works as far as it goes. So it's a deterrent to U.S. corporations and paying the bribes, it's a way of keeping people from doing the outrageous. On the other hand, most of the enforcement of that law has come out of self-reporting, which is to say the company or its auditors or its internal controls have come forward and said, look, we found these bribe payments and we confess.

It's very difficult to find those cases without the self-reporting, and then once the cases are prosecuted, there's the further problem. If a company comes forward and says, we paid bribes in Nigeria, the U.S. Government is in the terrible position of not being able to say who the bribes were paid to, for the simple reason that there's no proof that the person on the other end received it. What they know is the payments were made.

And I say in my statement, I have a very vivid memory of having a witness in a Foreign Relations Committee hearing talk about Prime Minister Seaga of Jamaica step forward—the witness said that Ciega had hidden bank accounts in the Cayman Islands. And I got back to my office and there was Prime Minister Seaga on the phone saying, wait a minute. How do I get to defend myself? I can't come as a witness to your hearing. And your guy who said I had these bank accounts was a convicted drug dealer. And I sat there and listened to myself being reamed out by the prime minister for the better part of a half-hour.

This is a very real problem. We will not be in the position of naming the people involved as a U.S. Government for that reason. On the other hand, do they have to be named? Do we have to figure out a way to stop this? You bet we do. And it's a real dilemma.

The most effective remedies in this area, because the criminal law is so fraught with these cross-border difficulties, and I can go into it in question and answer, the best solutions are in the civil arena, and that's what we talked about 7 years ago. And I'm pleased to say that in the intervening time, I have been working with Lord Daniel Brennan, who is a very distinguished member of the House of Lords, on putting together a civil asset recovery organization that will work across borders on behalf of countries that have now decided to try to recover the money. And this organization, I think, has the capacity to do what others don't, because it would be private and nongovernmental, and therefore wouldn't fall into the thorny messes that come when you have to deal with sovereign relations among states.

I see that my time has expired. Am I wrong about that?

The CHAIRMAN. Take an extra minute, because we only have one panel.

Mr. BLUM. The problem of civil recovery is it requires a lot of work in a lot of different countries. It requires many different sets of legal skills, and it requires a degree of non-interference by political players. And that's a very important extra piece. We have had too much interference by political players, even in the areas of criminal prosecution. And I give you as a couple of examples the Geffin case involving Kazakhstan, an indictment years ago of a gentleman who was supposed to be a bag man in some oil contracts. The case has yet to come to trial. The indictment is pending, and there's no explanation whatsoever for why this case hasn't come to trial. There have been delays and arguments that, well, maybe this man was somehow connected to our intelligence services, but not a shred of evidence has been put on a public record about it.

In the case of other countries where criminal prosecutions have gone forward, let's talk about the Nigerian case, the U.S. Government is currently delaying the mutual legal assistance because the

investigation is ongoing here in the United States. Now just understand the bribes in Nigeria took place between 1995 and 2002, 2004 perhaps. We're just going to finish up our criminal proceedings perhaps in another year or so.

But now the Nigerians get evidence that is 10 to 15 years old, and then there's the question of all the other countries that this case touched. So Halliburton had a partner in France. The partner in France worked with Halliburton to set up a company in the Portuguese island of Madeira. There's a French criminal investigation underway, and the assembly of all this evidence to make any sort of case in a Nigerian forum won't happen for another 5 years at the minimum. This is a kind of impossible situation. It's so far after the fact that the money will be gone and the defendants will be able to do all sorts of things with respect to statute of limitations and making their defense.

So I just stress that this is a very difficult and thorny process. We don't have any simple solutions to it, and I think a lot of work and discussion will have to go forward. I think perhaps some of the answers lie in tightening up know-your-customer rules, but even there we have a real problem.

Thank you.

[The prepared statement of Mr. Blum can be found on page 89 of the appendix.]

The CHAIRMAN. Thank you. Let me just begin, Mr. Blum, you mentioned because Ms. Lawson talked about naming and shaming as a major tool given some of the legal problems, but you point out there's a problem with the naming. Could we work out a procedure in committees where you would not release the name until the party had some chance at a rebuttal?

Mr. BLUM. Well, it's really tough. The first time we hit that was with the Lockheed case in Japan. We had hard evidence that the Prime Minister of Japan, Tanaka, had received bushels of cash money from Lockheed Aircraft to get their planes into Japan. The State Department was apoplectic. They said you can't do this. The Japanese are major allies of ours. This will cause a political earthquake in Japan, which it did do, and they wanted us not to hold the hearing. It took tremendous effort to then get the evidence to the Japanese, and to their credit, the Japanese actually did something about it. They convicted him and he went to jail. But there were many other countries we had evidence on, and the State Department didn't go anywhere with it.

The CHAIRMAN. Well, let me ask you, what if we try to work out a procedure whereby if we said in advance, let us know, and we would then notify the named individual and offer to release contemporaneously any rebuttal? Obviously you're not going to get the prime minister to come sit here. But I'm wondering whether you think that could—

Mr. BLUM. It's a possibility, but I don't really have confidence that the prime minister would be very happy or that the State Department would be very happy.

The CHAIRMAN. Well, I appreciate that, but State Departments are often unhappy with Congress and vice versa.

Mr. BLUM. I know.

The CHAIRMAN. What I'm trying to satisfy is not some diplomatic rule but our own standard of fairness. And I will say that we might want to work on something where with—that there has to be some notice, and there is then a chance to rebut, and if somebody decides not to rebut, they don't.

Let me now ask the general question, obviously, and Mr. Castle and I were talking about it, there's a great deal of support for doing away with the corruption, particularly, and I appreciate the extent to which we have emphasized, it damages our ability to alleviate poverty. It is poor children who are the major victims of the corruption. This is not a victimless crime.

We will be told, yes, but the problem is you can't put American businesses at a disadvantage. Ms. Lawson mentioned the level playing field. I will just make an aside on this. The level playing field, it's an extraordinary phenomenon, the unlevel playing field. It is I think the only one I can think of where it is an unlevel playing field and no one in the history of economics has ever been at the top of the level playing field. It is a constantly downward-sloping playing field, and people are only at the bottom. No one in the history of congressional testimony has ever acknowledged being at the top, or even in the middle of the unlevel playing field.

But that's the question which I will ask you to comment on briefly now. Help us figure out ways to diminish the disadvantage. Part of it, I think, would have to do where this committee has the jurisdiction, with the banking system, being frozen out of the American banking system could be tough. And Mr. Blum mentioned that people managed to sneak their way in. But I think you were suggesting with know-your-customer that we may be able to prefer to do that.

But I would just ask if one of you had any comments now, and I think we would be very open to what we could do to diminish the argument that we're putting Americans at a disadvantage. Mr. Baker?

Mr. BAKER. Thank you, Mr. Chairman. The same argument was made at the time the Foreign Corrupt Practices Act was being discussed, that it would badly damage U.S. business interests around the world. It did not. We may have lost the odd aircraft sale or the odd oil field service contract, but we certainly did not hurt U.S. business globally. It did take the Europeans another 20 years to follow suit, but that was an example of U.S. leadership that led to the rest of the world following as well.

And I said in my remarks, further U.S. leadership is needed. In fact, what we need to do now is to catch up with where the Europeans are. They have gone past us in the range of what is barred of monies crossing borders. We cannot successfully fight corruption while at the same time maintaining our financial system open to so many other forms of illicit money that go through the same such channels. Corruption can pass through the same channels as the flows of other forms of illicit money.

The CHAIRMAN. Ms. Lawson?

Ms. LAWSON. I would encourage the committee to focus on the role that the Financial Action Task Force could play in improving the standards elsewhere. The United States is one of the driving forces behind the Financial Action Task Force and has a lot of in-

fluence within it. At the moment, the naming and shaming that I referred to is not about individuals, it's about jurisdictions who do not have anti-money laundering standards at the appropriate level, and while FATF is spending some attention at the moment talking about some of the countries that are way out of line, most if its own members do not yet have standards fully in compliance with the levels that it sets. So that's one way that the United States can use its influence abroad.

The CHAIRMAN. Mr. Ribadu?

Mr. RIBADU. Thank you. Well, just to agree with her, the FATF did a lot of—

The CHAIRMAN. Move the microphone closer to you.

Mr. RIBADU. FATF changed Nigeria, and it has really made it possible for us to really address the problem, not just of corruption but so many other things. I think there is a need to look at the possibility of strengthening and helping it to get back to what it was a couple of years ago.

On the issue about the American business outside, as a person, a physical person on the ground in Nigeria, I can assure you that the Foreign Corrupt Practices Act did a lot of good to America, far, far more than what you can ever imagine. I investigated companies in Nigeria from 2003 to 2007. Wherever I see an American company is involved, doing business, I tend to be relaxed. I tend to believe that somehow they are far, far better than the rest of the world, not to talk of the emergence of the Chinese and the Indians.

The Foreign Corrupt Practices Act helped to build confidence, show direction, change the world perception, and it also helped us to raise our own standards. It may be the same thing that you are faced with today. Please do have the courage, understand that what you are doing, you are taking the lead. Whether it is going to be a temporary loss, I can assure you in the future you will see the benefit of it. Today, most of the companies from America are taking the benefit. They tend to be believed. We agree with them because of this oversight responsibility coming from their home country.

The CHAIRMAN. Thank you. Ms. Macovei, on the international coordination, is there anything we can do?

Ms. MACOVEI. I didn't understand.

The CHAIRMAN. Yes, if you had anything that you wanted to add on how we can—

Ms. MACOVEI. I would like to say as the others to insist on international cooperation. Exchange of information is vital, and I saw in some cases where information to not leave one state to go to the other through the law enforcement. And also I can say that I saw contracts, and without direct evidence of corruption looking at the terms of the contracts where all the rights were and all the duties were, it was a clear bad business for the state and good business for the company. But my point is probably companies who try to do these, the problem is the environment where they do the contracts. If a country provides this poor environment in which corruption is possible at the government level, then the company will take—

The CHAIRMAN. Well, in some cases you can just look at the terms of the contract and figure out that some money changed

hands because there would be no other logical explanation for those contract terms.

Ms. MACOVEI. Right. I made these examples because I saw contracts where there was no price. The price was going, for instance, to be decided by the contractor, by the contractor company.

The CHAIRMAN. Oh, very nice. Mr. Blum, any last word on this?

Mr. BLUM. A couple of thoughts. First on the issue of level playing field in the banking business, I think that if banks don't take this kind of corrupt money, well, they may be at a competitive disadvantage, but this is business we don't want them to touch. Moreover, when things go bad, the advantage is not to the people who took the bad money. So look at UBS, which took all this tax cheating money, that now has all of its customers fleeing because they're going to be exposed, and they're in terrible trouble. So I don't think that's the issue.

Now this business of the contracts, I think the issue here is price. If there's public exposure of the price and the terms, it gets to be very had to pad the contract to hide the bribe. And that is a very important aspect of keeping this process honest. So, for example, there was an infamous case in St. Maarten where a Sicilian contractor went into negotiation to build a new airport, and the price once they sat down with the people who were running the government of St. Maarten kept going up with consulting payments supposed to go to a company somewhere in Switzerland. Well, you knew what that was all about. Ultimately, the Dutch government got on top of it and did something about it.

The CHAIRMAN. Okay. Thank you. We will ask all of you, please feel free, and we'll be in touch about how we deal with this, because it is a practical matter that is going to be, I think, one of the issues we will have to deal with.

The gentleman from Florida.

I misread my things. The gentleman from Minnesota was first on the list.

Mr. PAULSEN. I will yield back, Mr. Chairman.

The CHAIRMAN. Then, the gentleman from Delaware.

Mr. CASTLE. Thank you, Mr. Chairman. I want to ask you something which I think is related to what we have been talking about, in fact, quite closely related. And that is the new trends in international terrorist financing, the new technologies in moving money around. Do we see scam charities or corporations playing a role in terrorist financing or even the corruption you have been talking about in foreign governments and should we be doing more and should the UN be doing more or is there some other entity out there that should be doing more? To any of you.

Mr. BAKER. Thank you for the question. In my own opinion, sir, the pursuit of terrorist financing has been a bright spot in these efforts. There were, shortly after 9/11, some 25 arms of the U.S. Government that were pursuing terrorist financing and as a result of that, I think that we have pushed terrorist financing out of the legitimate financial system. In my observation, as I study the issue, terrorists are moving their money through commodities, through drugs, through gold and so forth, but only to a rare extent using the legitimate financial system. There is some money passing through the Hawala system back into the hands of drug dealers in

Afghanistan and Pakistan that end up in Taliban hands. So, there is a linkage there. But, as far as terrorist financing in the legitimate financial system, personally, I think that U.S. leadership on this part of the problem was excellent.

Mr. CASTLE. Mr. Blum?

Mr. BLUM. The critical place to get at that sort of problem is in identifying shell corporations and in identifying who the beneficial owners of various trusts are. At the moment, under the know-your-customer rules, many financial institutions have been content to receive a copy of a corporate charter of an off-shore corporation, passport photographs of the local directors, and say, okay, the beneficial owner of the account is the corporation. That cannot be. We have to know who is underneath any shell entity that's coming into the U.S. banking system. And that is a fairly straightforward proposition, which will help us with tax collection, will help us ensure that terrorist money is out of the system.

Mr. CASTLE. Your answer is somewhat in contrast to Mr. Baker's answer, to a degree. You're basically indicating that shell corporations could be set up, you could use some sort of local director, take a picture, whatever, and accept the documentation and all of the sudden be able to fund through that—

Mr. BLUM. I don't know whether they would be used to fund, but I can say they can enter the banking system and their accounts can be used to move money. You know, where it goes or who it goes to, or what they do, is another issue. But used to move money, yes. And in the end, in the end, even the Hawala system uses the banking system, so you really want to know who the people are who are opening your accounts. And I think that's something that we have already talked about a lot in the area of the Bank Secrecy Act.

The banks and brokerage firms got a pass on identifying old accounts and then on the issue of identifying corporate accounts, the identification was left to saying, well, tell us who the directors are, and when you have a shell and you have shell directors, it doesn't tell you anything about the corporation. You have to know the beneficial owner.

Mr. CASTLE. Mr. Baker, can you respond to that? You indicated, obviously, in your statement, that we have taken a lot of steps to address the terrorist financing, etc. Mr. Blum points out the circumstance of being able to set up a shell corporation and avoid some of the niceties that might trip that up if it were to happen. Do we know that is not happening based on some of the things you have talked about or is it possible, it's obviously possible, but is it likely that some terrorist financing is taking place in shell corporations?

Mr. BAKER. It certainly can, sir. There is no evidence that I have seen that it is taking place. If I could make a further point about beneficial ownership. I strongly agree with my friend, Jack Blum, that beneficial ownership of entities needs to be known by every financial institution holding accounts. I made this point in New York recently and a Wall Street banker in the room raised his hand and asked, "Do you have any idea how much it would cost us to determine the beneficial owners of all of our accounts?" And of course, the answer is, it costs nothing. You put the shoe on the other foot.

It is the responsibility of the account holder to affirm who is the flesh and blood owner of the account or what is the listed company that owns the account. But this is a no-cost exercise and it should be done by all financial institutions. In this day and age of crime and terrorism, I cannot imagine a financial institution not wanting to know who are the beneficial owners of accounts with which they do business.

Mr. CASTLE. I thank you. My time is up. I would just say, in closing, that I agree with everything you have said about the problem. I worry about the solution on a broader basis in just the United States or just Europe. I think it's going to take a great deal of international involvement to get this resolved. I yield back.

The CHAIRMAN. The gentlewoman from California.

Ms. WATERS. Thank you very much, Mr. Chairman. I am very appreciative for this hearing that you're holding and very appreciative for the leadership and support of Mr. Bachus in dealing with this issue on corruption in the role of western financial institutions. We have been kind of picking around the corners of this for a long time. I recognize that we here cannot, perhaps, stop all of the corruption in the world, but I'm very, very concerned about our banks and financial institutions who participate in the support of corruption with acceptance of stolen money, drug money, on and on and on.

I would like to especially thank Mr. Blum for being here today. It seems as if he has been around the world with so many of these issues and I would just like to let him know that Mr. Ricky Ross, who was at the center of the crack cocaine scandal that was exposed by the San Jose Mercury is out, back at a halfway house in San Diego. Of course, as you know, Daniel Ortega, who was fighting with the Contras is in power now with the Sandinistas in charge. I don't know. It seems as if things just continue to rotate and that things don't really change that much.

But, here we are today again looking at this issue and whether it is a Halliburton that's involved in a bribery or any other American firm, or any American financial institution that knowingly accepts money from people like Abacha, and protect it, it seems as if we should be able to do something about that. I spent a lot of time on Citibank because they were obviously purchasing dope, little banks throughout Central America and Mexico and one of the brothers of a former president of Mexico, had a private banker at Citibank, who bought their homes and boats and all of that.

And that's what I think we can get a handle on. "Know-your-customer" does not accurately describe it. I mean, it has to be better than that. I don't think that the brother of the president of Mexico at that time even had a card on file to talk about where they lived, earned money, but they had a private banker who facilitated the purchase of all of these assets. So, what I would like to do is, I would like to find ways to stop our banks, period, from accepting a corrupt money and protecting corrupt money.

I would like to find out what the IMF and not only the International Monetary Fund, but the World Bank, they have a lot of investigations. And they have a lot of research information. They know a lot about some of these countries that are involved in deep, deep corruption and who are putting money in American banks. I

would like us to find ways to get access to the research they have and, of course, simply close down the ability for our banks to have this money placed in accounts in these banks. So, you have been giving us some suggestions. You have talked a lot about the know-your-customer rules. Is there anything else you would like to share with us about what we should be doing to close down the ability of American banks to accept this cash from these corrupt people? Yes?

Ms. LAWSON. In response to your points about the IMF and the World Bank, they have a very strong role to play in this. They play a significant part in the mutual evaluations, the peer reviews, that the financial action task force does of its members. When they got involved in 2002, it was on the condition that FATF stop naming and shaming, explicitly, the countries that did not have appropriate standards in place. So, if they were to be supportive of that, FATF could be made more effective in ensuring that there's a better global standard.

The other interesting role that the IMF and the World Bank can play is that in the analyses of countries' economies, the Article IV Reports, for example, for the IMF. There is information about the transparency over natural resource revenues and payments. Given that in many of these most corrupt countries, it is natural resources that are providing the money that can be so easily looted, more information made available in a very clear form, from the international financial institutions to the banks to help them in doing their due diligence to identify where the corruption might be taking place, would be very useful.

Ms. WATERS. Thank you very much. Mr. Chairman, let me wrap up simply by saying, we don't want to hurt the poor people who we are trying to support in these countries and I'm just sitting here thinking about how we cannot get the money to the governments that are responsible but rather to some NGOs or other to continue some of that work. And I yield back the balance of my time.

The CHAIRMAN. The gentleman from New Jersey was next on the list.

Mr. GARRETT. I thank the chairman. I thank the members of the panel, Ms. Macovei, Ms. Lawson, Mr. Ribadu, well, everyone, everyone on the panel for your work and the sacrifices that you have made on its behalf. You know, I think of the actions that Congress has tried to take in this, that I have been involved with, is trying to help the people. One prior to the Iraqi war situation, I was down on the Floor on a number of occasions when the whole issue of the now infamous oil for food scandal began to explode.

And there is, just as Ms. Waters says, the issue there is, where is the money supposed to go? It is supposed to go to the folks over there, the people over there, the poor people over there for food and medical supplies and other things and it didn't get there. And of course, we have now learned it went from, not just to Iraq, but political folks from Russia to France and in this country, all around the world. The discouraging part from my aspect was, in Congress we put in a number of, I put in a number of amendments to say, let's call for accountability, let's withhold some of our funds to go there, and quite honestly, they fell on deaf ears in this House because of the nature of what we were, others were trying to do.

But I think it was the right thing to do, to try to call even an entity like the UN, accountable for their actions. Now, the chairman raises the proverbial issue, I'll go along this line with regard to the level playing field. Ms. Lawson, I think you mentioned in your testimony with regard to at least one bank, Riggs Bank, and what happened there. Now, there is a case, just to tell you the other side, there is a case where the United States did have the tougher law.

We had the civil and criminal prosecutions. They had to basically sell out and what was the outcome of that, the outcome of that for them, not very good, outcome as far as in Europe and the rest of the banking world, they just continued on, right? So, even though we took the leadership position, what came of that? Ms. Lawson?

Ms. LAWSON. Thank you for your comments. I think that brings up a very interesting issue. It's very concerning that when the United States takes this very effective action using some of the powers that it has, that we then see a European bank continuing to hold an account for one of the characters involved and I would like to reassure you that in addition to coming here to seek leadership from the United States, we are also working, spending a lot of time working, in London, in Brussels, and in other European capitals to try and get European governments to look at this, as well.

But another issue that comes out of this is, let's look at the mansion that Teodorin Obiang owns, which is in the United States and was purchased in February 2006. Now this is after Riggs was closed. This money that he used to buy it, $35 million or thereabouts, must have come into the United States in some form or other. So, while it is very important to ensure that the European standards also improve by using the mechanisms that we have internationally, such as FATF, there may also be issues with money still being able to come into the United States somehow in order for this guy to purchase his house.

Mr. GARRETT. Well, you know, you raised the issue of the banks looking at, how do they have this much assets, I was thinking, I'm from New Jersey. We had a case where we had a prominent city mayor who made a city salary and he was getting, he had a large boat, several real estate holdings, and cars and everything else, so with the idea of looking at, not just the terrorist list, which you referenced, does that mean that we have to have a system where banks even within this own country have to start questioning if we have political figures that are getting all this aggregating of assets when they're only making X number of dollars as a city mayor or councilman or something like that, but that's their responsibility now?

Ms. LAWSON. As far as I'm aware, it's the bank's responsibility to ensure that they don't accept the proceeds of crime of whatever it is and that applies to their customers wherever they're coming from. Now, the strong, impressive work of this committee has led some regulations in the form of the Patriot Act, section 312, that apply to foreign account owners, in particular, as a specific means of tackling corruption. But, the anti-money laundering laws are basically the proceeds of crime. So, it's a bank's job to work out whether their customers' funds are legitimate, whoever they are.

Mr. GARRETT. Okay. Yes, Mr. Blum?

Mr. BLUM. I might add in this discussion, I represent financial institutions and work with them in compliance. I have actually sat with committees that look at questionable accounts and decide whether or not the bank will take them on or whether or not, after looking at some questionable transactions they want to get rid of the customer. And, in truth, the better institutions all recognize something called reputational risk. The presence of, let's say, the Obiang account is not worth the trouble that account will bring if we all understand that we're dealing with a significant crook. The problem comes when that crook comes into the bank through some kind of disguised means where the bank can't be certain that it's the crook and can't really question. Let's talk about a clearing broker who sees the transaction. The account originated with the introducing broker, now what do you do? Pick up the phone and say, we're going to fire you, the introducing broker unless you get rid of your customer? And that gets to be a lot tricker.

Mr. GARRETT. My time is up, thank you.

Ms. MACOVEI. Can I—

The CHAIRMAN. Yes, if the gentlewoman would like to answer, she may. We only have one panel, so we can be a little loose with time here.

Ms. MACOVEI. I think we should also think of the responsibilities of all the reporting agencies to the anti-money laundering financial needs. It's first the banks and they, as we all know, they have to report not only transactions over a certain value, but any suspect kind of activity or transaction. And also, there are responsibilities at least in the laws for notaries and for other categories of sort called deporting entities. So maybe you should also look at the framework and the obligations of these many others who know. Thank you.

Mr. GARRETT. Thank you very much. Thank you, Mr. Chairman.

The CHAIRMAN. The gentleman from Kansas.

Mr. MOORE OF KANSAS. Thank you, Mr. Chairman, and thanks to our witnesses for your testimony this morning. As a former district attorney, and the chairman of this committee's Oversight and Investigations Subcommittee, exposing corruption, fraud, and wrongdoing at both the local and Federal levels of government has been a top priority of my public service and I hope everybody on this committee's public service.

Today we're focusing on corruption and criminal acts at the international level. When the stolen funds can mean the difference between life and death for too many impoverished people, the need to crack down on these acts could not be greater. Normally, a government program is set up, funds are distributed, and we wait for enforcement at the end of the process and hope to catch any illegal acts that may have occurred. The Special Inspector General for TARP or SIGTARP has worked to move enforcement efforts earlier in this process with respect to the TARP program.

Mr. Barofsky last reported having 20 criminal investigations ongoing and has made it a priority to work with Treasury to build into their TARP program stronger accountability and transparency measures to prevent waste and fraud before crime happens. Can we implement the same approach for these international programs?

That is, increased transparency in the program and establish vigilant oversight at the beginning so we can catch possible illegal acts before the crime happens and becomes more widespread and I would like to hear from any of the witnesses who care to comment. Please. No comments? Mr. Baker?

Mr. BAKER. Congressman, what I would like to comment on is the question of what U.S. banks can take and what they cannot take.

Mr. MOORE OF KANSAS. Okay.

Mr. BAKER. The United States has two different lists. A very long list of domestic crimes of which we cannot knowingly accept that kind of money. The foreign list is a very short list. Basically, we borrow inflows from abroad of the proceeds of corruption, terrorist financing, and drug trading. Bank fraud is also part of that. But in my earlier remarks, I indicated all the other kinds of criminal activities the money of which can flow legally into the United States.

Now, if the receiving bank has a suspicion that the money is from a criminal source, it is expected to file a suspicious activities report. But, the key is, it can accept the money. It can take the deposit. The United States is one of the last countries to utilize a two-list system. Most European countries have gone to the definition of what constitutes laundered money, illicit money, as being the proceeds of a major crime. The UK has gone a step beyond that and called it simply the proceeds of a crime. If you knowingly handle the proceeds of a crime, you've committed a money laundering offense.

Congresswoman Waters asked for specific suggestions as to what needs to be done to address this problem. I would assert that until we close those loopholes by which other kinds of criminal money can come into the United States, we cannot effectively fight that component, which is corrupt money.

Mr. MOORE OF KANSAS. Thank you, sir. Are there any other comments from the witnesses? Yes?

Mr. BLUM. I would like to add a thought on this. The biggest problem that I see is the absolutely antiquated and impossible situation of information exchange and witnesses exchange. Let me give you an example. When we met as a working group at the UN to discuss the problems of prosecution and going after this kind of corruption, the prosecutors, the working prosecutors said, you realize we can't compel the attendance of a witness across international boundaries if the witness doesn't want to come.

There's no system for bringing them into the country with immunity to testify. The process of getting evidence across international borders is basically a bilateral business that takes months to accomplish. And if you get a lead in one place and then have to follow up in another country, you can be years in trying to develop even the simplest criminal case involving financial flows. So, one of the most important things we can do is find a global way of modernizing this absolutely antiquated bilateral system of one off exchange.

Mr. MOORE OF KANSAS. Even with the cooperation or willingness of the other country, where the resident resides? They can't compel that person—

Mr. BLUM. If the person is willing to come here as a witness, that's fine.

Mr. MOORE OF KANSAS. But I mean, the government of the nation where that person lives can't compel that person to go to our country?

Mr. BLUM. No. By and large it will be, the opportunity will be then given to perhaps have a deposition in the foreign country if it's a country that wants to cooperate.

Mr. MOORE OF KANSAS. Thank you. I see my time is up. Thank you to the witnesses.

The CHAIRMAN. The gentleman from Minnesota.

Mr. PAULSEN. Thank you, Mr. Chairman. Many changes to the transparency of the financial institutions have been made since September 11th and we have also seen an increase in efforts internationally to clamp down on financial crimes. There are currently some pretty heavy regulations on U.S. financial institutions and we can certainly debate whether or not those are sufficient, but I think there's still a heavy burden on U.S. banks. As I understand it, one of the areas where we are seeing some increase in fraudulent activities right now is with the new technologies that are going on. In particular, online payment systems and banking provide an easy opportunity to evade regulators in general. Can any of you comment, specifically, on that, on what might be targeted directly on that area in particular? Mr. Blum?

Mr. BLUM. There are some new technologies which are being used. Smart cards, cell phones, that offer opportunities, but in this issue that we're talking about today, grand corruption, they go the old fashioned way, which is plain old investment accounts and investment advisors and lawyers in Geneva and private bankers. They're not using high tech. And in fact, the problem is, that when they get this corruption money and they're still in power, there's no reason why anybody can't deal with it because there's nothing in the system that can say, don't deal with money you suspect being corrupt other than your own good nature.

Mr. PAULSEN. Mr. Baker?

Mr. BAKER. Congressman, the argument is often made that we cannot stop these kinds of illicit flows and use of cell phones and Smart cards is given as an example. I have long advocated that the goal is not to try to stop all corruption and all illicit financial flows; the goal is to try to curtail it. We can curtail it very substantially with a handful of measures. This won't completely end the problem, but the first goal should be to substantially curtail the literally hundreds of billions of dollars of illicit money and tens of billions of dollars of corrupt money that flow across borders. That can be done as a matter of political will.

Mr. PAULSEN. And Mr. Ribadu, I had the privilege of traveling to Africa also just 3 weeks ago with my colleague from Georgia, and it was stunning to spend some time in The Congo and see how aid is potentially not reaching the folks that it should be targeting, especially children and a lot of the IDP camps where we had a chance to visit. And I'm just curious, based on some of the comments you had in your statement where the African Union is reporting that corruption really is draining the region of something like $140 billion a year, 25 percent of the continent's official GDP.

In general, how much money of multilateral bilateral aid is reaching the citizens of a developing nation, realistically, at the level that it should be targeted to. Or what percentage of those extractive revenues is reaching those citizens? I guess, in other words, does much of the money pouring in from the G-7 or other organizations, is it targeting and doing much good where it should be getting to or is there another way to aid development if so much money is getting picked off the top or being stolen?

Mr. RIBADU. Thank you. Well, that is what the fundamental issue is. Basically, whatever that goes in, hardly will see the benefit of it. It's literally probably 20 percent, average, of what I have seen in terms of credit, it's international aid that goes in, for the money coming internally, chances are if you are lucky in some conditions, you could get fairly about 20 percent of the value. And that is really the issue.

And the problem we are talking about here and what I have heard so far, it seems as if we tend to look at from this point, we don't seem to understand what is going on, on the ground, where the corruption is happening. I have heard one person after another asking, what can the United States do? What could you do with your own institutions? We have to start talking about what could you do out there, where it is happening. You may take your own measures, you may take your own fantastic beautiful, whatever, it is not making any impact. But from where the corruption is taking place. I think it is high time to start looking at what are the possibilities of reducing whatever is making it possible for this corruption to continue.

Who are those responsible? What can be done about it? And I have seen from the experience of what I did in Nigeria, with a little effort of pushing, for example, the initiative of FATF, the Financial Action Task Force, that costs nobody nothing it makes massive impact in us having to change fast, set up a financial intelligence unit, have a control over all financial system, ability to also improve and raise our own standard and then it suddenly change the whole dynamics of corruption between the developing countries and the developed ones.

I think we need to have this type of thinking and direction, the United States giving more attention, more time, and more resources to this issue involving 400-something million people who are desperately poor. I can imagine if 5 percent for example of the initiative or the effort being given to some other parts of world, issues to do, for example, I'm sorry to say, maybe with Israel and the Arab countries. Israel and Palestine have 10 million people; Africa has close to 500 million people.

Please give us 5 percent of the time you are giving to Israel and the Palestinians, and you will see the difference it can make. Unless we start addressing the problem back home on the ground in Africa, trying hard to confront those who are responsible for this corruption, chances are you may continue to improve your own systems here, it is not likely going to be the solution. This is the direction I think we should start looking at.

Thank you.

Ms. LAWSON. Could I briefly add something to that? We have an interesting statistic here, which is that in 2007, the value of ex-

ports of oil and minerals from Africa was roughly $260 billion, which was nearly 6 times the value of international aid to Africa. Now, the fact that we're needing to give that aid shows that those natural resource revenues are not going where they need to.

What we see happening time and time again in every one of these natural resource rich but highly corrupt countries we investigate, is that aid is propping up the basic functions of government and providing legitimacy to the regime while they get on with the larger and more lucrative business of stripping the state of its assets. Now, if that aid is going to be undermined until we stop the incredibly damaging illicit flows that are coming back out into the rich world.

Now, I'm interested that in Congressman Bachus' testimony in 2002, that committee, he said, it's a concerted international effort involving close cooperation among regulators, law enforcement authorities and financial institutions is absolutely essential for dealing effectively with future Abachas. Now, here we are 7 years on. Perhaps some of those future Abachas are being talked about in this room today.

And as far as we can see, in addition to the international problem, it's not completely clear from what we have looked at, that the U.S. regulators have a handle on exactly what it is that U.S. banks are doing to fulfill their requirement to identify the beneficial owner of their customer. There's a good framework in place there, but the specifics of whether it is working properly do not seem to be clear.

So, we would encourage this committee to inquire of the Treasury what it is doing to ensure that it and the U.S.'s regulators fully understand whether the U.S. banks are fulfilling this requirement in a meaningful way and whether further explanation is needed in the second deregulation to make it absolutely explicit and to make these regulations meaningful so that they're used effectively.

The CHAIRMAN. Mr. Scott?

Mr. SCOTT. Thank you, Mr. Chairman.

In trying to get our hands around this in terms of what can we really do about this situation, and I think that if we focus on the banks, we regulate the banks, the banks could be an area. Let me just ask: Do any of you know any United States banks who are engaged with accepting corrupt customers? All right. Perhaps you do and do not want to mention. Let me ask you this then.

Because if we are not willing to face the truth and say that U.S. bank are engaged in accepting corrupt customers, then we all need to just dismiss this panel and go home. What are we doing here? Our number one function is regulating our banks. Now, we know one thing, Mr. Baker. You have mentioned that once a bank receives, so there are banks who are receiving what they comprise as a suspicious customer, and then you said that that bank must require that a report be filed and submitted for the suspicious customer, but they still take the money.

That appears to me like a get-out-of-jail-free card. If they suspect it's a suspicious, corrupt customer, then why do we have this loophole here for them to say just file a report, but go ahead and take the money. And they filed the report just in case it shows up that they're corrupt. Well, hey, we have a chair to sit in here when the

music stops. I got the report I filed. It seems to me that we ought to be able to do something about that. But now, let me ask you this. When they get the report, they file the report. Where do they send the report? And then secondly who is overseeing this? Who do they report the report to? They just file a report and it sits there?

Yes, Mr. Blum?

Mr. BLUM. A problem is, yes, they file a report. The report then goes to the judicial district where the most activity relating to that report exists, and then there's a committee of law enforcement agencies that sit and decide whether anybody wants to pick up on it and make the case.

Let me assure you that with thousands of reports and all sorts of prosecutorial possibilities, no agency is going to step forward to go after a foreign leader's corrupt money case to figure out if there's a violation of U.S. law they can prosecute; and, as a result, because it's time consuming, sticky, difficult. They take the easy stuff, and these cases don't go anywhere.

Mr. SCOTT. So what can we do about this? We have on the books two major laws: the Bank Secrecy Act; and the Foreign Corrupt Practices Act. Is that sufficient? I mean what can you tell this committee that specifically the Financial Services Committee needs to do to tighten this?

Mr. BLUM. Well, first and foremost, as I said earlier, it's essential that every bank know the beneficial owner of these offshore entities they're dealing with, and that doesn't mean getting passport photographs of a board of directors sitting in Nevus. It means actually finding out where the heart, the mind, and the brains of whatever entity it is exists and who it is. And, that way, they can't shrug their shoulders.

The institutions can't shrug their shoulders and say, "Well, we really didn't know that was money coming from Abacha, or it was coming from somebody else who is robbing this country blind." They will then have the specific knowledge; and, the beauty of that is that then the institution will confront reputational risk. But I have to give you caution. I'll give you the case of a wonderful fellow who was the Mexican ambassador to the United Nations, who suddenly found Citibank closing his account because of money transfers from Mexico. And the money transfers, they were his salary.

There is a flip-side to all of this, and that is that the people who have the accounts and the people who have legitimate business have to be able to sort of respond and say, wait a minute, this is legitimate.

Mr. SCOTT. All right, Mr. Baker, really quick.

Mr. BAKER. One of the steps that needs to be taken is substantially strengthening "know your customer" requirements. At the present time, a U.S. bank receiving money from a foreign depositor is expected to satisfy itself that the money is not derived from corruption, drug trafficking, or terrorist financing. That's the extent of the questions that need to be asked.

If that individual walks in and says, "I make my money by smuggling aliens from one part of the world to another part of the world, but not into the United States," a U.S. bank can take that money. It would be expected to file a suspicious activity report. I think the last that I recall, there were some 12 million to 14 million sus-

picious activities reports filed a year, so you can imagine how few of them get addressed.

The last time, and we're talking what—1999—when "know your customer" was put on the table in an attempt to strengthen regulations. At that time, it was made equally applicable to American and foreign account holders, and it was not legislated successfully, because it broached privacy concerns of U.S. account holders.

There is no reason why we can't strengthen "know-your-customer" requirements as applied to foreign account holders and require, not on a judgmental or voluntary basis, the kinds of questions that bankers are expected to ask. Put "know your customer" questions, requirements, into a much more regulatory framework. The following questions have to be asked. Preceding all of that as I stressed again must be the passage of legislation that says all those kinds of criminal money are not acceptable in the U.S. financial system.

Mr. SCOTT. Thank you.

Mr. BLUM. I would like to, if I may, add one.

Mr. MEEKS. [presiding] Really quick; the gentleman's time has expired.

Mr. BLUM. The real thing you could do would be to change commercial banking law so that the bank becomes a constructive trustee for money that it knows is derived from a fraudulent source, so that the bank then carries the civil law responsibility if it forwards the money to somebody other than the genuine, beneficial owner. So in the case of money stolen from Nigeria, that would be the Nigerian people. But if it forwards the money on to buy a mansion in Malibu, let's say, they would be liable for passing the money on. Make the banks commercially responsible under civil law and you take a huge step forward.

Mr. SCOTT. Thank you very much.

Mr. MEEKS. The gentleman from Florida.

Mr. POSEY. Thank you, Mr. Chairman, and first I also want to commend Chairman Frank for bringing forth this issue to the light of day. Listening to the comments of course, the consequences are heart-wrenching that are described in your testimonies; and, to put things in a proper perspective, I mean we have to realize that there are a lot of legal protections that we take for granted in this country that aren't really relevant in another country, I mean, to own and transfer property to go into business in a timely manner.

I mean, just a whole lot of things, not to mention the civil and human rights protections we have that so many people around the world right now are unable to enjoy. And while reading through the remarks of course those of the first four speakers, they gave us your testimonies in order and so we look at them in order. The thought comes to mind that there might really be a legitimate beneficial place for the UN to do something as an international crime-fighter until I read about Mr. Blum's experiences with the Transnational Corporations Act of 1976 and how that was just blown away and laughed off apparently.

And given the fact you have to realize this country was given the heads-up 10 years ago about Bernard Madoff, and, nonetheless, the people we have to enforce those laws turned a blind eye or a deaf ear to that and allowed him to plunder $70 billion, which makes

your thieves in your countries look like a bunch of small town crooks.

And, so, you say, wow; you know, can there be any hope? Can there be any hope? But I think fortunately right now there still is some focus and everyone seems to agree that these activities that are used to fund terrorism are not going to be tolerated anywhere, except of course by the terrorists themselves. And I think that the inhumane treatment, the human misery that's caused by this corruption that can maybe, at least through mutual partners or mutual banks, be tied to funding of terrorism might be the link, might be the answer that it's going to take to get some action.

You know, it's not going to be a unilateral action by the United States taking sanctions just against our banks or our wrongdoers. It has to be more international and bilateral, and multilateral, and like your comments on how you think that might work, because I see that maybe as an open door for you.

Ms. LAWSON. And if I might respond to that comment, I think you're right that the key to this is in what is being done to focus on terrorist finance in the system, and it's very clear. And I think there's pretty much agreement on that, that all forms of dirty money flow through the same system. So if we don't close the system to the types of dirty money, all of them are going to come through.

The key to this, I think, the key to illustrating it is this extraordinary document we have in our report and the stories I touched on very briefly. I have more detail in the written testimony about Denis Sassou Nguesso, the son of the President of Congo, and his extraordinary designer credit card shopping. We have a map of his shopping route through Paris and the report.

Mr. POSEY. I read all that, but the focus still sounded drilled down.

Ms. LAWSON. This document has been stamped, "Record of Terrorists Checked." This shows that there has been a focus from the international community, pretty much led by the United States, to make sure that a bank in Hong Kong—it's called Bank of East Asia—I'm not even sure if anyone here would have heard of it—it's stamping that document, a payment credit card instruction, "Record of Terrorist Checked."

Now, we need to use the same mechanisms that have made that happen to say, so that that bank is stamping that document, "Record of Politically-exposed persons checked," to make sure that they have done their due diligence into whether they're dealing with a politically exposed person. The same mechanism that is being used to do that can be used to focus on corruption. This isn't a matter of technical difficulty or of the huge amount of new regulation that's required. It's a matter of political will.

Mr. BLUM. One of the things that has been left out of the discussion this morning is some obvious cases where the corruption is undermining U.S. national security interests in a major way. So, Afghanistan, there's a huge flood of drug money back. That drug money isn't walking there. There's a system that's moving that money. There's a lot of money involved in that. We have yet to get our arms around it and, likewise, in Iraq there's massive corruption and we haven't really gotten our arms around what's hap-

pening there; and, in both cases, it's undermining our national security interests.

Now, this is for a lot of reasons. Most of the heroin in Afghanistan winds up in Western Europe. The Western European countries are not dealing with drug money laundering. They're very good at certain other things, but in this area, the failure of cooperation among the European countries, has allowed that money to flow back. Now, this is all part of the same problem we are talking about. It's part of the corruption because the drug money is going back to pay corrupt government officials. It's undermining our most important strategic goal at the moment. So we really have to find way to tackle these problems, and as I say, it's not easy, and it's something we just have to put a lot more work into.

Mr. MEEKS. The gentleman from Texas, Mr. Hinojosa.

Mr. HINOJOSA. Thank you, Chairman Meeks. Thank you for giving me the opportunity to ask some questions.

I want to thank all the panelists, because I think that you all have given us some very interesting information and I too want to join Chairman Frank and Ranking Member Bachus in acknowledging the neverending quest of Chairwoman Waters to combat poverty in Haiti and corruption in foreign governments, particularly in developing countries.

Congresswoman Waters has helped me considerably in my congressional district on various issues and I am glad to participate today. I agree with Chairman Frank's assessment of what we have heard this morning from the panelists. He describes the problem of corruption as an unlevel playing field for have-nots who continue to be disadvantaged on this playing field.

So my first question is directed to Mr. Ribadu. My question is in two parts. First, it seems to me that you contend there is approximately $93 billion currently in the markets supporting corrupt governments. If $93 billion is the accurate data, how did you arrive at that number. Second, what substantive and credible evidence do you have that American companies, government contractors and our financial institutions are helping developing countries to loot moneys and public assets by public officials?

Mr. RIBADU. Thank you. The first question on the $93 billion, it comes from the Europe and United Kingdom Commission for Africa. They came up with that figure. They said that about $93 billion stolen from Africa is divided to different financial institutions across the world. So it came from the U.K. authorities.

On the issue about the American companies, let me share with you the fact that American companies probably are the best in the world today if you compare with the rest of the world. I have seen it in Nigeria. Partly because of what you are doing, no other country in the world is doing what you are doing. For example, Congress calling the whole world to come and share with you what the experience, and you have most of the stringent legislations. It is working. It has helped greatly. It's just not America benefiting from it. We are the first in terms of benefit, and I would want to encourage you to go that direction, improve on it.

The challenge is what also can you do on ground where it is happening. For example, I wanted to suggest about the Foreign Corrupt Practices Act. If there would be a possibility of extending the

sanctions, not just to the American companies and individuals from America who do give bribes to foreign countries and foreign business entities, but what can you do about those who are the receivers. As long as you continue to get those who are beneficiaries of this corruption and they continue to get away with it.

Mr. HINOJOSA. Excuse me for interrupting you, Mr. Ribadu.

I don't want you to answer my question with a question.

Mr. RIBADU. Yes, sir.

Mr. HINOJOSA. Just give me credible evidence that our American companies are doing what you said.

Mr. RIBADU. Halliburton, Parnanpena, Zenith, in the last 2 years, the Justice Department cut it out, investigation into close to about 20 companies doing business in Nigeria and they also put sanctions to the tune of over a billion dollars. But nothing is happening to the other side, those who made this money, and they are still very big, powerful individuals in Nigeria, and they will be continue to be there. And, as long as they are there—

Mr. HINOJOSA. Thank you. Time is running out and I want to take advantage of this opportunity to ask another question directed to Mr. Baker and Ms. Lawson.

I realize that drafting legislative language is not your specialty, but what language would both of you recommend that we on this committee, with the support of Chairman Frank, use to draft and move through regular order?

Mr. BAKER. If I could give you what in my opinion is the first and most important step, and that is to change the range of predicate offenses under anti-money laundering legislation to include all forms of criminal money coming from abroad. As I have explained, we are currently very selective in what we bar coming from abroad. That needs to be changed. We cannot alter the reality of corrupt money flowing into the U.S. banking system, while at the same time being open to so many other forms of illicit money.

Senator Grassley, who endorsed the back of my book along with Senator Levin, has in fact in the last legislative session and in the preceding legislative session, put a bill on the table that does exactly that.

Mr. HINOJOSA. Thank you.

I want to hear from Ms. Lawson. What is your recommendation?

Ms. LAWSON. I would encourage this committee to push for some more explicit language around Section 3–112 of the Patriot Act, which is the bit about requiring due diligence on the beneficial owner of foreign accounts opening accounts here, to make it explicit that not only should the bank be required to identify the beneficial owner, but they should have evidence that the funds are not corrupt, else they should not accept them.

Mr. HINOJOSA. Thank you for those specific responses, and I yield back, Mr. Chairman.

Mr. MEEKS. Mr. Miller.

Mr. MILLER OF CALIFORNIA. About time you recognized me, my friend.

I have enjoyed the testimony today. We have talked about laws that we have in the Federal Government and who is responsible for implementing those laws.

And we talked about United States banks and if a bank, you know, accepts illicit money, knowing that that's one thing; but when a bank files a suspicious report, they're saying, "We're asking if this is legitimate or not."

And we talked about liability for such actions and such. But if a bank does that, they're sending a need to the Federal Government or to a government agency that has jurisdiction. And then I think responsibility falls on us at that point in time, the government agency or the Federal Government, to respond to that bank.

I want to move very cautiously in the direction of saying that bank is bad, because they did what they were supposed to do, and if the money is not only suspicious, it is illicit, they have done their job.

And I would want to move cautiously in areas where we are going to say we are going to hold the bank liable for something that they did that they were supposed to do.

But Mr.—is it "Ribadu?"

Mr. RIBADU. Exactly.

Mr. MILLER OF CALIFORNIA. I was right, he was wrong. I thought it was "Ribadu," he said "Ribadu."

Mr. MEEKS. No, I said "Ribadu," and he said—

Mr. MILLER OF CALIFORNIA. No, you blew it, I'm not buying it. You talked about Halliburton—

Mr. MEEKS. The gentleman's time has expired.

Mr. MILLER OF CALIFORNIA. Well, don't get personal.

[laughter]

Mr. MILLER OF CALIFORNIA. I tried to get in the Black Caucus and you wouldn't let me in. That's why he's trying to get even with me.

[laughter]

Mr. MILLER OF CALIFORNIA. You talked about Halliburton doing business in a country, and it sounded like the country was extorting Halliburton if they wanted to do business in that country. Is that what you were saying? And Halliburton paid money and went to some illicit group or government agency that was wrong or improper?

Was that what you were saying?

Mr. RIBADU. Exactly.

Mr. MILLER OF CALIFORNIA. How was that Halliburton's fault?

Mr. RIBADU. The fact that they gave money—

Mr. MILLER OF CALIFORNIA. Well, the fact is that a business wanted to do business, and they're saying "Unless you pay us—we're a corrupt government—we're not going to let you do business."

Mr. RIBADU. Yes. That—

Mr. MILLER OF CALIFORNIA. So who are you pointing the finger at, I guess—

Mr. RIBADU. That is the sad story of the whole thing. And that is what is really going on. It's not just Halliburton.

Mr. MILLER OF CALIFORNIA. Yes, but whose fault is that?

Mr. RIBADU. Unfortunately, those who are in charge of foreign affairs—

Mr. MILLER OF CALIFORNIA. Is it not the person who is in charge of extorting the business?

Mr. RIBADU. But it is the responsibility of the company doing the business. Also, what they could not do back home, they are also not entitled to do outside.

If you behave very well in your own jurisdiction, chances are it is expected that you should also extend the same thing to wherever you go.

You cannot, for example, do a different—

Mr. MILLER OF CALIFORNIA. I understand. But what do we do, let's say, if an American business is trying to do what they're in business to do business in the country, and the country basically their leadership is extorting that business.

The American business can—they have two choices. They can say, "Fine, we're not going to do business, and we're going to let somebody from France or Germany or Japan or wherever do business over there, because they're going to play by the illegal questionnaire rules."

I mean, I think we need to be getting at what countries are doing this, and how do we really deal with those? But how can we ensure that the policies to prevent exploitation from financial institutions and businesses by these corrupt figures are really implemented comprehensively? And how do we do that globally?

I know, Ms. Lawson, you're looking at me with a question.

But the reason I ask you that question—and you get that look on your face is: When I was a young man, I had a HUD official do that to me as a business person, as a contractor. We were doing business in Los Angeles County, my partner and I; I was in my early 20s and he was in his late 40s.

And we had a HUD director in Los Angeles call my partner into his office, close the door, and say, "Unless you give me a third of your profits in advance, when you issue the contract, you're not going to get the work any more."

And my partner came back to me, and I said, "Well, he can't do that, because this is a government agency, and we have a right, we're on a bid list to bid the job." And I thought, you know, I was being extorted, and I said "No."

And I'm going to put myself into a position to Halliburton. Well, every contract we bid on after that, that we were a low bidder on, they found a problem with the RFP, and when they re-did the RFP, we were not on the bid list for the second one.

So we were a company—and I was a young guy—who would have said, "We're not going to do that, we're not going to fall to corruption," even if it was a director of HUD back in those days.

Halliburton is in the same situation, and other American companies are in a situation, where they go and they say, "Well, we want to bid on your job, and we bid appropriately. And you're telling me that if I don't pay you off, I don't get the job, and this is an American company doing business in a foreign country."

And my opinion is, the contractor is the innocent guy. He just had the stupidity or whatever you want to call it, integrity, to say, "No, you can't do that because you're a government agency and I can bid on it."

But I never got another job. So the American companies are stuck in the same situation. And my question is: How do we make

sure that we adopt policies that not only apply to the United States, but apply globally?

Mr. RIBADU. Yes. Well, let me just explain this little thing: Corruption and bribery is a criminal act.

Mr. MILLER OF CALIFORNIA. Yes.

Mr. RIBADU. It's not different from, for example, murder, rape, or kidnapping. Do you think just because others are doing it, it is okay for you to go into it? No.

I think the first step, the first position is to say, "No, I'm not a criminal, I'm not going to do it—

Mr. MILLER OF CALIFORNIA. But what country was it you said Halliburton was having to pay off?

Mr. RIBADU. Excuse me?

Mr. MILLER OF CALIFORNIA. You mentioned a country you said Halliburton was having to pay off.

Mr. RIBADU. Well, in the case of Nigeria, about—

Mr. MILLER OF CALIFORNIA. What country was that?

Mr. RIBADU. Nigeria.

Mr. MILLER OF CALIFORNIA. Who were they paying off?

Mr. RIBADU. Nigerians.

Mr. MILLER OF CALIFORNIA. And who's in charge of—

Mr. RIBADU. Unfortunately, that is the case, but—

Mr. MILLER OF CALIFORNIA. Prosecuted—

Mr. RIBADU. The desperate poor of Nigeria are the ones who are at the receiving end, not the very few who are privileged to be in charge of the affairs in Nigeria. That's why the issues is: What can you do as a country, as good people of the world? As leaders. What do you do to help be on the side of the 140 million desperately poor Nigerians?

Or do you think it is okay for profit to stand in conspiracy with a small group of Nigerians who benefit from this, and then cheat, short-change, and literally turn—

Mr. MILLER OF CALIFORNIA. I think it's wrong—

Mr. MEEKS. Let me let Ms. Lawson—and then we're going to be out of time.

Ms. LAWSON. I hate to employ a cliche, but it's the most relevant way of doing this. The cliche is, "It takes two to tango." And that is the best one that we can apply to corruption.

Of course, there are a small minority of people in Nigeria and in a number of other countries in the developing world and indeed sometimes in the developed world, who wish to employ corrupt means to do what they want do to.

But they cannot do it without the involvement of businesses to pay bribes and of banks to take the money that either comes from the bribes or comes from people having their hands in the till.

Corruption cannot take place on this scale, without the facilitating services provided by the rich world. And we are being inconsistent in our policies towards these countries, if we don't make sure that we and our businesses and those that we regulate are not complicit in doing that.

The other thing to point out is that there is a set of international norms and domestic laws in the United States, which make everything that you're talking about illegal.

Mr. MILLER OF CALIFORNIA. And I agree with everything you have said—

Mr. MEEKS. I'm going to let Mr. Blum go, and then that's going to be it—

Mr. BLUM. I want to just throw in this thought. If I were representing the company, but had the demand made for payoff, I would go to the U.S. Embassy, explain what was happening, and insist that my government step forward to both make representations to the Nigerians. And then, because I know who else is bidding, to make representations to the other governments about, "Well, these guys are bidding, and we think they're involved in payoffs, and why don't you ask about it?" and get at that level immediate cooperation in shutting that game of payoff down.

Now in the case of Halliburton, what happened was the U.S. company worked with a French company and they cooperated together in paying the bribes.

That was not the approach. The approach should have been: Talk to your governments, use the international agreements, and then put pressure on the Nigerians to say, "Cut it out."

Mr. MEEKS. Mr. Baker?

Mr. BAKER. Congressman, I have done business all over the developing world for 35 years before I segue'd into the think tank community. I lived 15 years in Nigeria, and spent another 20 years doing business all over the rest of the developing world.

You can do business without indulging in corruption. You may lose the occasional piece of business, which I have done, but I have no regrets over the business that I have lost.

We're not going to revisit the question of whether or not it is illegal to bribe foreign government officials. That is U.S. law. There is no excuse for any U.S. company doing so.

Mr. MEEKS. The gentleman from Colorado, Mr. Perlmutter?

Mr. PERLMUTTER. Thanks, Mr. Chairman. And this really has been a fascinating conversation.

Mr. Miller, your questions were good ones, because the way I see your testimony, everybody, you have a couple things going on here. One is: You want the banks to be the traffic cops, and it involves illegal sales or illicit sales, so drugs. It involves bribery and extortion, and it involves theft—somebody just stealing from the country's treasury in some fashion or another.

So you have three things. You would like to expand kind of the laundry list that banks look at. Ms. Lawson would like to have another box to check, which would say, "Is this a political person? And why does he own the house in Malibu, you know, when he should only be getting $5,000 a month?"

And so, Mr. Miller's question is, "Okay, does this only apply to the United States, or do we have a global banking system? So, you know, it's Wells Fargo. Are they—Wells Fargo is the only one that looks at this? Or does the Bank of East Asia?"

How do we, if we're going to do something, expand the list of laundered funds, and expand the list of people that you look at; how do we get this to other countries? That's number one.

And then Mr. Blum, I have a second piece, which is I am actually working on an amendment to the Foreign Corrupt Practices Act that tries to bring in more of the civil side of things, so that if, you

know, company X feels like it was hurt by a French company that did, in fact, bribe somebody, that company X could go get a lawyer, try to bring a civil lawsuit, and recover monies under the Foreign Corrupt Practices Act, that it isn't just the Federal Government's.

So I want to start with you, Mr. Baker. How do we make all the banks traffic cops? Or do you want to start with U.S. banks?

Mr. BAKER. The first step is for the United States to catch up with where the European countries are.

Mr. PERLMUTTER. Okay.

Mr. BAKER. Most European countries have passed laws stating that it is illegal to knowingly receive the proceeds of a major crime. We are not in that position yet. We need to catch up with the European—

Mr. PERLMUTTER. A major crime would be drugs sales, bribery, extortion, theft?

Mr. BAKER. No. It's the same list in almost all European countries, the list that applies to domestic crimes. And that is usually any crime that carries the punishment of a year or more in jail—

Mr. PERLMUTTER. Okay. A felony.

Mr. BAKER. A felony.

Mr. PERLMUTTER. All right.

Mr. BAKER. It's against the law in almost all European countries to knowingly handle the proceeds of a felony offense, whether that offense was committed in country or out of country.

Mr. PERLMUTTER. All right. Ms. Lawson, do you agree with that?

Ms. LAWSON. Yes. I would agree with that. And I would reiterate the point that the way that these mechanisms can be expanded to the rest of the world is the way in which the United States has already required the rest of the world to come along with it in the war against drug trafficking and the war against terrorist finance.

Both of those were led by the United States and it used the Financial Action Task Force to ensure that other jurisdictions had similar standards in place.

And while it's a bit clunky at the moment, they're not all quite there, it's definitely bringing them along. So that is the mechanism that you use to ensure that the international community as a whole turns against the proceeds of corruption.

We're dealing with global flows of money. It would be absolutely pointless for the United States to do it on its own.

Mr. PERLMUTTER. Okay.

Mr. Blum, what do you think about private rights of action and getting the civil community into this? If my company has been hurt because somebody else bribed, I didn't get the job. I want to sue somebody.

Mr. BLUM. We already have unfair methods of competition rules under the Federal Trade Commission Act, and this is certainly an unfair method of competition.

The biggest problem is going to be getting the evidence and the witnesses and the material, especially if this has happened outside the United States, and then finally getting a U.S. court to decide, "Yes, we have jurisdiction and that this is the right forum to hear it."

Because until now, a lot of international cases that have involved questionable activities wind up being thrown out on the ground of

forum non conveniens. The judge just simply looks at it and says, "I don't need this horror show in my court room, this is the wrong place. Go sue somebody in France or in England."

Mr. PERLMUTTER. So then, what you're saying is not only do we have to change the law, to expand it, but we're going to have to have some treaties that allow for witnesses to be obtained—

Mr. BLUM. Yes, and this business of exchanging information and evidence is critical, especially given the timelines.

I mean, my experience in trying to get the Justice Department to respond now to turn over Halliburton-related evidence to the Nigerians is an illustration of that. We are now 10 years out on the case. And they haven't begun to turn anything over.

Now who knows what will happen to it on the other end? That's not the issue. The issue is: Can they get started? And this is a very complicated case involving multiple players, multiple countries. And you have to produce evidence and you have to produce evidence beyond a reasonable doubt.

Mr. PERLMUTTER. Okay. Thank you. My time has expired.

Mr. MEEKS. The gentleman from New Jersey, Mr. Lance?

Mr. LANCE. Thank you, Chairman Meeks. Good morning to you all. I have found the testimony compelling. And I think it's very disturbing, and I hope that we can work together in a bipartisan capacity on this issue.

Mr. Ribadu, you indicate in your testimony that you would recommend a proposal on an international proceeds of crime treaty. Could you flesh that out to a greater extent for me as to how that would work? And would that require a statutory change here in Washington? And among others across the world?

Mr. RIBADU. Thank you, sir. First, I wanted to also say something with respect to what the U.S. authorities have done so far to bring this international cooperation.

Nigeria is a very good example today. We do have a financial intelligence unit, that has helped greatly to improve our own financial system. And it came as a—support from FINCEN. FINCEN is an American outfit with responsibility of regulation.

We have Edmund Group. Edmund Group is a group that is involving financial intelligence units in the world, where we share information and through that we are able to advance the work we are doing.

It has all been promoted and supported by the United States and the U.S. Government.

I also wanted—I may not be, but just understand where I'm coming from—I'm coming from Nigeria, Africa—maybe not part of your own system here—but I wanted to see the possibility of not just America going after those who are giving the bribes, in the case of corruption; but what can you do also, the receivers who are out there? Because nothing is happening to them.

Of all the 60-something cases that have so far been taken under the Foreign Corrupt Practices Act, not a single case has been where you have a punishment of the receiver. Unless something is done, then nothing is going to happen to them.

In Nigeria, the Halliburton people who made money from it, are still our rulers. If you go to Congo, the same thing. If you go to almost all the other countries, as long as—

Mr. LANCE. What would you recommend to change that situation?

Mr. RIBADU. Is it possible, for example, to have an amendment or have a new law that says: If you receive money from an American company or an American entity, you have supported an American company in the commission of a criminal act involving corruption. You are also subject to the American control and judiciary, and therefore you can be punished.

And America is powerful, I can tell you. America, the moment it takes the step, the rest of the world comes along. I have seen it. Almost all the work I have done as a physical investigator, I have seen what American authorities have done.

The case of Halliburton, I followed it as far back as 2003. I went and met the magistrate in France, who refused to support me, who refused to help me, who refused to assist me on this case. I took the case to UK, I did not get the support. I brought the matter to the US, here. And the U.S. authorities took it. And since then, we have seen the difference. In several other cases, it has always been so. I am very, very passionate about the steps, the actions America usually takes.

That is why we believe that if there is hope to address this problem of corruption, it is likely going to be coming from America.

Please take that and recognize the fact that the world is having these high hopes and expectations. You can do it by making the laws. You can do it by expanding your—you control MasterCard today. You control VISA. All these transactions go through such companies.

If you want to go after the son of the—he uses a Mastercard. That alone gives you jurisdiction and control. The laws in America ought to be expanded to cover these areas.

Thank you.

Mr. LANCE. Thank you. Would others on the panel like to comment on what has just been said regarding the fact that we seem to be doing something right, but there is this situation regarding other countries—the countries that were mentioned, France and Great Britain—because obviously we can't fight this battle alone.

Mr. BLUM. Well, I think that we have signed a variety of conventions. There is now a Global Convention Against Corruption. There is an EU Convention Against Corruption. There's a Latin American Convention Against Corruption.

So the problem isn't that there aren't international agreements. The problem is that in our legal system, all criminal matters are matters for the individual state. And one state can't push another state to prosecute people. We can't step across borders to prosecute crimes in other countries. And that issue of sovereignty becomes an enormous barrier to being able to do what you really want to do.

I mean, in the United States we solved all of this by having a Federal Bureau of Investigation, that could actually take on individual corruption in individual States. We had a Federal system that could step in to deal with cross-border crime.

In the rest of the world, that doesn't exist.

And when these agreements are negotiated, every country, including the United States, is terribly careful not to impinge on the sovereignty of any other country.

So every one of these agreements doesn't say, "Here is what the law should be." It says, "You will pass your own laws in accordance with this general framework."

Mr. LANCE. Thank you. Thank you, Mr. Chairman. I yield back the balance of my time.

Mr. MEEKS. Thank you. And just before we adjourn, I think I heard in the beginning of this hearing, Ms. Waters make a statement in regards to concerns, because we want to make sure that those developing countries don't lose out on funding. We want to make sure.

And I, along with Mr. Miller, who is my ranking member—I chair the Subcommittee on International Monetary Policy—we just had a hearing last week in regards to or following up from the meeting in London with the G-20, where now we know that there is going to be a substantial amount of money, close-bordering on a tree in Dallas, going through the IMF, who is going to play a significant role in it.

My question to you is: Number one, do you see or have you seen in the past any dollars as it pertains to IMF or the World Bank, find its way through the corruption of others, so that it has not reached the hand that it's supposed to? Is there a complicity with regards to some American as well as other banks, especially in Africa and Asia, where some of the IMF money may flow through, to get to the various countries?

So that's a real concern to some. Let me just throw that question out really quick.

Mr. BLUM. I would say that you should remember what happened the last time the IMF had a lot of money to give to a country in trouble, it was Russia. The money wound up in a bunch of bank accounts offshore on the Island of Jersey. There was an audit report that talked all about it. The audit report was posted on the Web, but when the moment came to discuss it, it mysteriously disappeared, because the Russian government protested.

The problem with both the IMF and the World Bank is the same sovereignty problem I have been talking about, which is they will do nothing to step on the shoes of a sovereign country that says, "We won't."

And it makes following up on anything very, very difficult. It makes following up on issues of corruption and disappeared IMF money and disappeared World Bank money very difficult.

The World Bank is still struggling to figure out how to deal with the obvious cases of corruption, where the money that it has lent has simply disappeared and the project doesn't exist.

Ms. LAWSON. There's a small practical step that the IMF and the World Bank can take when they're dispersing funds for any kind of, say bailout or development projects, which is that contracts are signed with officials in the government of the recipient countries. And if these are the people who are responsible for administering the project, then these are the people who have the potential, if they're going to be corrupt, to be accessing these funds for the wrong purposes.

Now, a very practical step that the IMF and the World Bank could do, would be to make the names of those officials with whom they sign development contracts available to the companies that

run the politically exposed persons lists. So that when the banks are doing due diligence on their customers, these people who are potentially at very risk of diverting funds are known to the banks, and they can feed that into their assessments of whether they might be dealing with somebody corrupt.

Mr. BAKER. Overseas development assistance has for the past several years been running about $100 billion a year from all sources: World Bank; the United States; the EU countries; Japan; and so forth. About $100 billion a year.

Contrast that generous distribution of foreign assistance going into developing countries with our estimate of the amount of illicit money that comes annually out of developing countries. As I said to you, we have done a report utilizing standard economic models, and estimated $1 trillion a year of illicit money coming out. In other words, for every one dollar that we are handing out across the top of the table, Western countries have been receiving back some $10 in illicit money under the table.

There is no way to make this process work for anyone, the developing countries or the Western economies themselves.

Mr. MEEKS. Mr. Ribadu?

Mr. RIBADU. Thank you. Well, there are changes that have taken place at the World Bank and the IMF, which has changed considerably in the last few years. They have been able to improve their own internal systems and capacity.

What I want to see happen now is let the governance and integrity packet that they have been able to develop now to be part of every transaction in their relation with any country that they are dealing with. Let it be central. Unless you are ready to do good governance, unless you are ready to open up, unless you are ready to make transparent every detail of the work you are doing, we are not going to deal with you.

And I believe it is going to force these countries to change. The United States could also help by freeing the money that you can support the World Bank and IMF. Countries in Africa are in dire need of this support.

America is the biggest of the supporters, and we need you to free this money and help them. The World Bank has changed right from Mr. Wolfowitz, the former president, up to Mr. Zoellick. We have followed what is going on; I can assure you it has changed considerably. It is already making massive impact in Africa. Almost all the new sort of relations that they are having, they put it at the center the need for openness, transparency, accountability, good governance, abuse of rights, and generally promotion of democracy. Hopefully maybe that may be the biggest change that will come to the developing countries.

Mr. MEEKS. Thank you.

And I want to thank all of the witnesses for being here and for testifying today. Be assured that Chairman Frank has indicated that we will have a follow-up hearing where this committee will be looking at possible laws and regulations that can be put in place to try to stamp out the kind of fraud that has been taking place.

I also note that some members may have additional questions for this panel, which they may wish to submit in writing. So without objection, the hearing record will remain open for 30 days for mem-

bers to submit written questions to these witnesses and to place their responses in the record.

Again, we thank you.

And this hearing stands adjourned.

[Whereupon, at 12:25 p.m., the hearing was adjourned.]

A P P E N D I X

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The Context within Which Corruption Thrives And How to Curtail the Global Problem

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THE CONTEXT WITHIN WHICH CORRUPTION THRIVES AND HOW TO CURTAILTHE GLOBAL PROBLEM

By Raymond W. Baker
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Thank you Mr. Chairman, Ranking Member Bachus, and members of Congress and the Committee. I appreciate the opportunity to appear before you today.

In 1977, following outrage at revelations of bribery by American businesspeople overseas, the United States signed into the law the Foreign Corrupt Practices Act, barring Americans from bribing foreign government officials. At the time there was widespread concern that this might place U.S. businesses at a competitive disadvantage. While we may have lost an occasional aircraft sale or oil field service contract, there is no evidence that the U.S. economy was hurt by our nation taking this principled stance. And though it took most European nations another 20 years to follow our lead, eventually anti-bribery laws became widespread and now are accepted as an essential component of responsible global business practice.

Having said this, there is today no evidence that the dollar volume of corrupt money has declined. On the contrary, it appears that corruption may be at the highest levels ever, particularly with very large sums of money shifting out of China and Russia, while flows likewise continue out of Africa, Latin America, the Middle East, Asia, and states in the former Soviet Union.

How can this be? With so many nations adopting anti-corruption statutes and so much attention given in multinational organizations to fighting corruption, how is it possible that corruption may in fact be on the rise? To answer this we must place the issue of corruption into its larger context, the global shadow financial system and its attendant culture of opacity.

Since the 1960s, we in the Western world have created and expanded an entire, integrated global financial structure to facilitate the movement of illicit money across borders. There were a few elements of this structure available before the 1960s—four or five tax havens and the use of abusive transfer pricing techniques. But the 1960s marked the takeoff point in building this structure for two reasons. First, it was the decade of independence. Between the late 1950s and the end of the 1960s, 48 countries gained their independence from colonial powers. Some of the economic and political elites in these newly independent countries wanted to take their money out by any means possible, and we in the West serviced this desire with a great deal of creativity. Second, the 1960s marked the decade when multinational corporations began their aggressive expansion all over the globe. Yes, there were international businesses before the 1960s, but typically an international oil company or trading organization might have branch operations in only some 12 or 15 foreign locales. Beginning in the 1960s corporations rushed to plant their flags all over the planet, a process that continues today. Many of these corporations utilize aggressive tax avoidance and tax evasion strategies to shift their profits around the globe, a process again serviced by the shadow financial system. So for these two reasons—decolonization and the spread of multinational corporations—the 1960s marked the point when the development of this shadow financial system accelerated.

This system now comprises a number of elements:

- Tax havens are a major part of this structure, now 91 in number around the globe.
- Many tax havens also function as secrecy jurisdictions, where entities can be set up behind nominees and trustees such that no one knows who are the real owners and managers.
- Disguised corporations, now numbering in the millions around the world.
- Flee clauses, enabling nominees and trustees to have disguised entities flee from one secrecy jurisdiction to another in the event that anyone comes seeking to find out who are the real owners of such entities.
- Anonymous trust accounts.
- Fake foundations.
- False documentation in trade and capital transactions.
- Falsified pricing in import and export transactions, by far the most frequently used element in this structure.
- Money laundering techniques.
- Holes left in laws of Western nations which serve to facilitate the movement of money through the shadow financial system and into our own economies.

Regarding this last point, for example, in the United States it remains legal to bring into this country proceeds generated abroad from handling stolen property, counterfeiting, contraband, slave trading, alien smuggling, trafficking in women, environmental crimes, all forms of tax evading money, and more. Having initiated the anti-corruption effort, we are now far behind our European counterparts in the range of illicit monies that we bar from entering our country.

This global shadow financial system moves cumulatively trillions of dollars of illicit money across borders. It equally facilitates the shift of the proceeds of corruption by foreign government officials, the proceeds of criminal activity such as drug trading and racketeering, the proceeds of terrorist financing, and the proceeds of commercial tax evasion. Some estimates suggest that as much as half of global trade and capital transactions pass through this shadow financial system somewhere between origination and completion. All forms of illicit money move on the same rails through this system, meaning that it is virtually impossible to interrupt one form while at the same time facilitating other forms.

Global Financial Integrity has recently completed an analysis of illicit financial flows out of developing countries, utilizing well accepted economic models including the World Bank Residual Method and IMF Direction of Trade Statistics. Ours is the first study to take these models and apply them to the whole of the developing world. In our analysis we show that somewhere between $850 billion to more than $1 trillion a year of illicit money flows out of developing countries, through the shadow financial system, and ultimately into our Western economies.

This massive outflow of illicit money from developing countries is the most damaging economic condition hurting the global poor. It drains hard currency reserves, heightens inflation, reduces tax collection, worsens income gaps, cancels investment, hurts competition, and undermines trade. It sets back poverty alleviation efforts and forestalls attempts to reach sustainable economic growth. Quite simply, it contributes in a major way to the environment in which corruption thrives.

The essential purpose of the shadow financial system needs to be clearly understood. This business is about moving money from poor to rich. It moves money out of poorer developing countries into our richer Western economies. And within our Western economies it moves money out of the hands of poor and middle income tax payers and into the hands of non tax payers with wealth ensconced in tax havens and secrecy jurisdictions. This system is, at its core, about shifting money from poor to rich.

Now how can we address these problems, both the larger problem of global illicit financial flows and the specific problem of corrupt money flows? What can we do?

Two preliminary points need to be noted. First, the goal should be to curtail the flow of illicit and corrupt money across borders, not to try to stop it. Stopping it would require draconian measures. Substantially curtailing it can be achieved with a few broadly adopted and widely implemented measures. Second, achieving this goal is a matter of political will. Some may argue that the process is extremely complex and technically difficult to accomplish. This is not correct; it is a matter of political will.

Three measures can substantially curtail the cross-border flow of all forms of illicit money.

First, financial institutions around the world should be required to know the beneficial owners of entities with which they do business. It is inexcusable in this day and age of terrorism and crime for any financial institution to conduct activities with a disguised entity, to fail to know for whom it is handling money. This is a no-cost exercise. Account holders are simply required to identify the flesh and blood owners of the accounts or the listed company that owns the account, in the absence of which the account will be blocked or closed. The U.S.A. Patriot Act provides an example of how effective such an approach can be in the way it largely removed shell banks from the shadow financial system. The Patriot Act established that it is illegal for any U.S. financial institution to receive money from a foreign shell bank, that it is illegal for any other financial institution in the world to send money to the United States that it has received from a foreign shell bank, and that this includes wire transfers that might touch New York City correspondent bank accounts for a moment before speeding off elsewhere. In other words, with a stroke of the legislative pen, shell banks were almost completely removed from the shadow financial system. The same process can remove remaining disguised entities from the shadow financial system.

Second, it is time to institute automatic exchange of key elements of information across borders, including for non citizens their earnings on accounts. The European Union Savings Tax Directive is a model for this process, requiring within the EU automatic exchange of information on non citizens of their earnings on bank accounts and certain other assets. Under consideration within the EU is extension of this agreement to include more forms of income and more entities, such as corporations, trust funds, and foundations. Automatic exchange of information would be a major contribution toward curtailing the worst excesses of the global shadow financial system.

Third, country-by-country reporting of sales, profits, and taxes paid by multinational corporations would do more to curtail the shadow financial system and the culture of opacity than any other step. Currently, corporations compile country-by-country information for internal purposes but do not provide disaggregated data in annual reports, Hence we see tens of billions reported in profits and little or nothing reported in taxes. Country-by-country reporting will resolve this problem and introduce more transparency into the global financial system than any other available measure. It is currently being studied by the International Accounting Standards Board and by the UK Treasury Department. Country-by-country reporting has a number of very significant advantages. It costs corporations essentially little or nothing, since they are

already doing it, just not reporting it. It is self enforcing because no corporation can report losses in country after country around the world, massive profits in tax haven entities, and yet little or no taxes payable. It utilizes the power of transparency rather than requiring a large regulatory regime. It curtails regulatory and geographical arbitrage. It contributes to making the accounting profession honest. It reverses the shift over recent decades of tax burdens off of capital and onto labor. And in doing so it reverses the growing inequality between rich and poor, a process that cannot continue without generating strong voter discontent. Finally, it can generate more revenues for strained governments than any other mechanism. For curtailing the harmful effects stemming from the global shadow financial system, country-by-country reporting is the most effective step available.

To address corruption per se, three additional steps are recommended.

First, we should harmonize predicate offenses under the anti-money laundering laws of all countries cooperating with the Financial Action Task Force (FATF) in Paris. This means that the United States should and indeed must adopt the European practice of barring knowingly handling the proceeds of criminal activities. It is unacceptable that the United States lags so far behind the rest of the industrialized world on this issue. U.S. facilitation of corruption cannot be ended while we at the same time are legally open to receiving the proceeds of handling stolen property, alien smuggling, trafficking in women, and much more. Closing these loopholes is long overdue. Furthermore, the FATF should add knowingly handling the proceeds of tax evasion to its list of predicate offenses. The U.S. Treasury Department has expressed its support for this inclusion, and, given the current global financial crisis, there is no better time to take this step than the present.

Second, strengthened Know Your Customer regulations as they apply to foreign account holders need to be implemented. Presently, KYC policies vary widely across financial institutions and even among account officers within financial institutions. KYC has been treated as recommendations rather than requirements. This needs to change. Adding a specific point on Suspicious Activity Reports for corruption is required. Again, the FATF in Paris should adopt comprehensive norms for KYC policies and survey and report on their adherence in cooperating countries.

Third, lists of Politically Exposed Persons—PEPs—should be available for all countries receiving development assistance, and use of PEP lists should be required by financial institutions. In the fight against corruption there is no better expenditure of aid money than this. Where reporting bodies in countries do not exist, they should be created and funded by bilateral aid agencies cooperating with each other and with developing countries. It is unacceptable that, following the corruption of Mobuto, Marcos, Suharto, Abacha, and others, we should today be confronted with the corruption of a new crop of leaders and family members robbing their countries, leaving misery and deprivation in their wakes, yet transferring their ill-gotten gains into willing Western accounts, properties, and assets.

The fight against global corruption is not being won. It cannot be won while at the same time maintaining a shadow financial system that moves trillions of dollars of other forms of ill-gotten gains around the world.

In the fight against corruption specifically and illicit financial flows generally, it is time once again for strong U.S. leadership.

Attachments:

1. Baker, Raymond, Christensen, John, and Shaxson, Nicholas. "Catching Up With Corruption," *The American Interest*, September/October 2008.

2. Kar, Dev and Cartwright-Smith, Devon. "Illicit Financial Flows from Developing Countries: 2002-2006," Global Financial Integrity Program of the Center for International Policy, December 2008.

Catching up with Corruption

Raymond Baker, John Christensen & Nicholas Shaxson

In the 1990s, mainstream development theorists and aid agencies finally began to accept the reality that if they wanted to know why some states fail, or why so many countries are tormented by persistent poverty, they needed to factor corruption into their equations. The Berlin-based Transparency International (TI), founded in 1993, deserves much of the credit for this shift. TI launched the first of its famous Corruption Perceptions Index (CPI) series in 1995, and the *Financial Times* took the cue by nominating that year as the International Year of Corruption. The World Bank, which had previously all but banished the "c" word from its policy documents, followed TI's lead after its President, James Wolfensohn, accepted in a landmark 1996 speech that the Bank needed to deal with "the cancer of corruption." Now the Bank considers corruption to be the single greatest obstacle to economic and social development in the world. The ripple effect from this change of heart has magnified the profile of the problem throughout the diverse fields of international development policy.

By any measure, this is good news. As many iconoclastic critics of business-as-usual development policy argued as long as half a century ago, ignoring the broad social and political frameworks within which economic policy exists is like expecting a fish tank to hold water without a bottom or sides.[1] Corruption is universal, but its forms vary considerably across different societies. One would have thought, therefore, that serious social scientists and practitioners of economic development policy would have factored it into their understanding early on.

They did not, however, thanks in large part to the way that academic economics shifted theoretical gears and methodologies after World War II. What had always been called political economy solidified its separation into political science and an economics profession, which was driven toward macro approaches in an effort to "harden" itself methodologically. The result was a sharp positivist, quantitative bias that by definition ruled out serious consideration of factors that could not be readily measured—corruption being, almost by definition, such a factor. To this bias was soon added what can only be called a condescending deference to newly independent countries: It was considered impolite, as well as unhelpful to certain parochial institutional interests, to delve too deeply into untoward behavior by the elites of newly sovereign and proud countries.

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[1]See, for example, Peter Thomas Bauer, *Economic Analysis and Policy in Underdeveloped Countries* (Cambridge University Press, 1957).

This explains, at least to some degree, the otherwise astonishing fact that it took half a century to acknowledge the role corruption plays in the dysfunctional economies of so many poor countries. It explains why the OECD's Anti-Bribery Convention entered into force only in 1999, and the UN Convention against Corruption not until 2003. In many developed countries, bribes were tax-deductible until just a few years ago. Whether it was grasping kleptocrats stealing billions from the state or disheveled policemen extorting bribes at roadblocks, the problem should have been diagnosed and dealt with decades earlier.

Not only has the world been slow to wake up to the problem of corruption in development, the World Bank and others leading the global fight against corruption have yet to accept the full and very inconvenient implications of this shift in thinking. The time is long overdue to re-imagine what we mean by corruption and to launch phase two in the battle against it. The task is not just to recognize the importance of a "supply side" to corruption, involving bribe-givers as well as bribe-takers; it is also about dramatically expanding our understanding of what the supply side has come to include in a rapidly changing, globalizing world. Only after our understanding has caught up with reality will we be able to adequately answer a question that has long puzzled economists: Why does so much money flow from poor countries to rich ones when, for both rational and ethical reasons, it ought to flow the other way?

Several recent developments suggest that a more mature understanding of the problem and the early stages of a phase-two response are already in train. A seismic shift came this past November when Cobus de Swardt, the new head of Transparency International, said that his organization would embark on a "second wave" of corruption campaigning to direct more attention to the responsibilities of Western governments and companies, and highlight their role in international corruption. The World Bank has recently dipped its toes into these waters, too. Last September, the Bank and the UN Office on Drugs and Crime launched the Stolen Assets Recovery initiative, which focuses on returning ill-gotten gains deposited abroad to their countries of origin. More generally, we see signs of an awakening among a variety of media, non-governmental and other groups about the harm caused by massive illicit financial flows and facilitating secrecy jurisdictions. We seem to be at the start of a long process that, if successfully pursued in the face of bitter opposition by vested interests, will ultimately accelerate global development and improve security for poor and rich countries alike.

Something Is Missing

We have a ways to go to match our understanding of corruption to a world of accelerating change. Corruption harms three main sets of actors: businesses, governments and citizens, especially the poor. The corruption concerns of these three sets of actors overlap significantly, but they are not identical. The dominant mode of thinking about corruption is shaped around the concerns of businesses. For that reason it tends to focus heavily on bribery, while ignoring much bigger problems.

For example, Transparency International's Corruption Perceptions Index has not caught up to TI's new resolve to surf the second wave. It draws heavily on opinion within the business community. While it does provide an invaluable ranking for investors trying to assess country risk, it is of little use to the citizens of oil-rich Nigeria, for example, to be informed by the CPI that their country is among the world's most corrupt. Nigerians and others like them want to know where their money has gone.

Consider the brutal Nigerian president Sani Abacha, who died in 1998, allegedly in the company of Indian prostitutes, but not before he had raked off billions of dollars of oil money from state coffers. Or to take a more recent example, we now know more or less how relatives and associates of the former Kenyan President Daniel arap Moi diverted hundreds of millions of dollars into their pockets through a web of shell companies, secret trusts and other evasive structures. Two jurisdictions that happily soaked up the embezzled wealth of both regimes are worth highlighting: Switzerland and the United Kingdom. "The UK authorities and banks", the BBC reported after a bit of the money was eventually returned, "were found to

have been even less cooperative than the Swiss, despite the latter's long and sullied reputation for protecting allegedly stolen assets." But despite these scandals and many similar crimes that have yet to surface, the latest CPI ranks Switzerland and the United Kingdom as among the world's "cleanest." Swiss and British rulers may be personally clean, but what about Swiss and British bankers, lawyers, accountants and, yes, even some lesser officials, who handled and harbored these stolen funds? In aiding and abetting grand theft and national-scale looting, they were knowingly complicit in, and therefore a necessary part of, the corruption process.

What Is Corruption?

It is fine that the CPI helps clean businesses assess the risk in doing business abroad, but what about some help for everyone else? To fight corruption that hurts governments and citizens as well as businesses, we need a comprehensive practical definition of it. The "official" development world is not there yet.

The World Bank defines corruption as "the abuse of public office for private gain." The restricted focus and the obsession with the public sector illustrated by this definition is both arbitrary and insufficient. Transparency International says that corruption is "the abuse of entrusted power for private gain." This definition is better, as it could be used more broadly, but in practice it is usually interpreted in a narrow way, notably by focusing on the public sector, particularly on bribery. Four classes of examples show why these definitions are inadequate.

First, during the dot-com euphoria of the late 1990s, Wall Street investment banks offered stocks in "hot" initial public offerings (IPOs) to corporate executives, who in return would then direct their own companies' business to these banks. Meanwhile, the bank analysts wrote glowing reports about the IPOs, while privately referring to them with terms like POS (piece of shit). The aim was to induce an inflow of corporate business and generate big fees. A second example is the widespread practice of illegal market rigging: Private companies build up secret monopolistic positions using shielded offshore structures to hide the fact that several apparently unrelated parties are in fact related and are colluding to fix prices. Neither class of cases involves public office or entrusted power. However, the first arguably involves a form of bribery, while the second violates laws of most Western countries.

Third, consider the byzantine Elf Affair, an eight-year judicial investigation launched by the French investigating magistrate Eva Joly that has been described as Europe's biggest corruption investigation since the Second World War. The "Elf Affair" involved, among many other things, oil money from the African subsidiaries of the then-French state oil company Elf Aquitaine being routed via tax havens and used to covertly finance French political parties and offshore slush funds in support of French diplomatic objectives around the world. The Elf Affair was echoed by the BAE Systems scandal, involving alleged corruption in British arms sales to Saudi Arabia. This was another thoroughly transnational undertaking linking oil-producing and oil-consuming countries, in which British Prime Minister Tony Blair invoked the "national interest" as a reason for allowing alleged corruption to go uninvestigated and unpunished. These affairs, too, which

Eva Joly

have provoked widespread disaffection among French and British voters, do not fit the standard corruption definitions because they are not primarily motivated by private gain, but by national security and policy considerations.

Fourth, many think corruption is always illegal. Not so. In the 1990s, Angola operated a system of multiple exchange rates through which well-connected officials could change local currency into dollars at a highly preferential exchange rate, effectively getting dollars on the cheap. Then they changed the dollars back into local currency on the black market, pocketing the difference. This amounted to free money for oil-rich elites, limited only by the number of hours in the day and the energy individuals had to indulge their greed. Although entirely "legal", the scheme was clearly corrupt, and it hurt citizens unable to queue up in that particular line. The point is that the system itself was corrupt, not just the actors, and it was not illegal because the same actors who created the scheme and benefited from it were also the ones who determined what was and was not legal.

If standard definitions fail to tell us what corruption really is, then what new definition do we need, and how should we create it? We should, above all, trust our intuition. Just as Potter Stewart was sure he knew pornography when he saw it, even if he could not define it precisely, so corruption should be defined as whatever corrupts: We know it when we see it.

We can do better than that, however. As a first step, we need to expand the geography of corruption. This is because corruption has not only a demand and a supply side, but also a host of intermediaries who facilitate the murky deeds. The sensible general strategy for fighting the international drug trade by tackling users, suppliers and middlemen is applicable to the global struggle against corruption. Thus, it makes no sense to see corruption through the prism of discrete, country-level problems. For example, the CPI ranks the countries of Africa as the primary locus of corruption, but it ignores the global infrastructure of international financial secrecy that has helped bleed trillions of dollars in illicitly generated money not only out of Africa but also out of the Middle East, Latin America and Russia into the financial centers of the richest countries in the world.

This reflects one of the most important fault lines in the ongoing process of financial liberalization, and it shows vividly why we need to see the big picture to deal even with the small snapshots. While capital has become almost totally mobile, the ability to police cross-border flows of illicit money remains severely constrained. International borders act like semi-permeable membranes, letting the crooks and the dirty money through while stopping the forces of law and order seeking to foil them. "The magistrates are like sheriffs in the 'spaghetti westerns' who watch the bandits celebrate on the other side of the Rio Grande", said Eva Joly after the Elf Affair. "They taunt us and there is nothing we can do." She was furious about the blocking role played by numerous tax havens, most especially "the City of London, that state within a state that has never transmitted even the smallest piece of usable evidence to a foreign magistrate."[2]

Beyond scaling up our perspective to the global level, we also need to pay attention to systems and processes, not just individuals. And we need to include consequences, not just methods. Corruption always involves narrow interests abusing the common good. It always includes insiders using guarded information operating with impunity. And it always corrodes institutions, worsens absolute poverty and inequality, and ultimately undermines faith in the rules and systems that are supposed to promote the public interest. Thus, a better basic definition of corruption would go something like this: *Corruption is the abuse of public interest and the undermining of public confidence in the integrity of rules, systems and institutions that promote the public interest.*

This definition is not limited to developing country kleptocrats and rogue officials, but makes room for a much broader array of actors and their facilitating activities. It also suggests a rubric for rich and poor to find common cause in fighting this global scourge.

That said, it helps to use the noun "corruption" sparingly and instead to emphasize the verb "to corrupt." Using the verb shifts our focus away from situations, people, isolated

[2]Joly, *Notre affaire à tous* (Les Arènes, 2000).

acts and finger-wagging, and toward examining underlying systems, relationships and processes. Markets and governments are built on trust, and the undermining of trust is arguably the greatest danger that confronts global markets today. Globalization can be a force for good, but it is tainted by a widespread perception that the system is rigged against ordinary folks. If countries retreat into protectionism, as some fear will happen, the sense of unfairness that stems from corrupting influences in the international financial system will have been a major contributing factor.

There are many consequences of refining our perceptions of corruption. One is that tax evasion is identified as a form of corruption, even if it does not involve the abuse of public office or entrusted power. While those people and institutions dedicated to tackling corruption today tend to focus on the theft of certain types of public assets, tax evasion is generally overlooked even though evaded taxes are stolen public assets, too. Tax evasion also looks very much like more traditionally defined forms of corruption because it involves abusive activity at the intersection between the public and the private sectors. It allows sections of society to bypass accepted norms, and provides one set of rules for the rich and well-connected, and another set for the poor and weak. It involves insiders operating in secret, without restraint. It corrodes governments.

Furthermore, the proceeds of tax evasion, along with the proceeds of bribery and criminal activities, use exactly the same mechanisms and subterfuges as they shift across borders: dummy corporations, shielded trusts, anonymous foundations, falsified pricing, fake documentation and more, all abetted by a supporting array of mainstream bankers, lawyers and accountants. Dirty money in many forms welcomed by the United States and Europe allows the proceeds of drug trafficking, racketeering, corruption and terrorism to tag alongside. These are parallel rails on the same tracks coursing through the global financial system.

Tax evasion is also the tail of a much larger creature: the cross-border capital flows that underlie it. The secrecy that facilitates tax evasion and other crimes is one of the most important reasons why capital flows out of capital-starved economies, a fact that orthodox economic theories cannot explain.

Expanding our definition of corruption will also change priorities in the field of foreign aid. Taxes, not aid allowances, are the most important and the most sustainable sources of finance for developing countries, whose long-term goal must be to replace foreign aid dependency with tax self-reliance. Aid makes governments accountable to donors; taxes make governments accountable to their citizens, and tax evasion undermines this basic pillar of civil accountability. As South African Finance Minister Trevor Manuel recently noted: "It is a contradiction to support increased development assistance, yet turn a blind eye to actions by multinationals and others that undermine the tax base of a developing country."[3]

And it is not just developing countries that suffer from tax evasion. Take the case of GlaxoSmithKline, which paid $3.1 billion after it settled a dispute with the U.S. Internal Revenue Service in September 2006 over transfer mispricing, the practice by which related subsidiaries of companies deliberately misprice internal transactions so as to cheat tax authorities. If tax evasion in all its forms is brought into the corruption debate, that means tackling the international infrastructure that allows developing and developed countries alike to be cheated of not just their taxes but of investment capital that exits to the secrecy jurisdictions.

Magnitudes and Measurements

There may be a clear theoretical case for launching a phase two battle against corruption, properly defined, but is it really worth pursuing? How big is the problem?

Precise measurement of corruption in all its forms is difficult: Transnational illicit financial flows and abusive tax practices are fragmented, hard to define and cocooned in a pervasive culture of secrecy. But if we start with a few things we know or can make educated guesses about, it will become apparent that the scale of this phenomenon is staggering.

[3]Address to the forum on tax administration, Cape Town, South Africa, January 10, 2008.

According to the OECD, more than half of all cross-border trade is routed through tax havens.[4] The World Bank's Stolen Asset Recovery initiative estimates the cross-border flow of proceeds from criminal activities, corruption and tax evasion at between $1 trillion and $1.6 trillion per year, about half of which comes from developing and transitional economies. This dwarfs foreign aid, which totaled about $50 billion a year through the 1990s and is about $100 billion today. So we have $50–100 billion of aid flowing into poor countries, and $500–800 billion of dirty money flowing out. In other words, for every dollar Western governments have been handing out across the top of the table, crooked Western banks, businesses and middlemen of various descriptions have been taking back up to ten dollars of illicit proceeds under the table.

On a different tack, the Tax Justice Network, using data from Boston Consulting, McKinsey, Merrill Lynch/Cap Gemini and the Bank for International Settlements, estimates that the world's high net-worth individuals hold around $11.5 trillion offshore, generating potential tax losses of $250 billion annually. This conservative estimate includes both legal and illegal tax dodges but excludes many other kinds of abusive financial flows. Even if one believes that the tax rates of some countries are extortionary, there is no excuse for, in effect, stealing public money that poorer citizens will end up having to replace. Tax evasion on such a scale is not only stealing from governments, it is stealing from ordinary people's futures in an act of reverse-Robin Hoodism.

What To Do

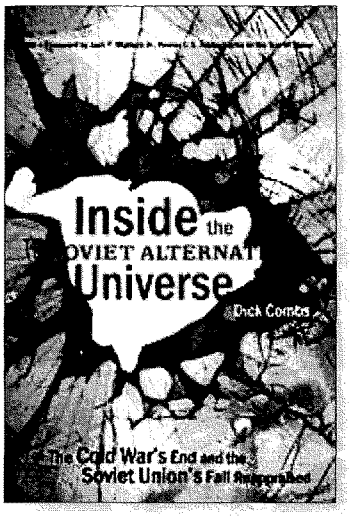
Now that we better understand the problem and grasp its magnitude, the questions turn to policy. What should we do as individual nations and as a global community? A look at the past will perhaps provide some guidance.

Policy has tended to trail behind galvanizing events. The U.S. Foreign Corrupt Practices Act (FCPA) of 1977 followed both the Watergate scandal, which helped create the right political climate, and a series of investigations revealing that more than 400 corporations had admitted paying $300 million to foreign government officials to win projects. Yet the FCPA did not trigger a decisive shift in global policy debates, since other countries did not follow America's lead. After 1977, companies from Germany, France, Britain and other countries still did business as before, gleefully corrupting foreign and domestic officials to steal contracts from under the noses of their more squeamish American competitors. It seemed inconceivable that genuine global cooperation on corruption was possible. What is more, the presence of secrecy jurisdictions allowed American companies to drive a coach and horses through the FCPA by enabling foreign corruption to continue to take place under the veil of offshore operations.

The Cold War played a powerful role, too. During that era, many on the Left, as well as others racked by post-colonial guilt, sought to blame rich countries and rich corporations for poverty and conflict in places like Nigeria, Indonesia and Nicaragua. Many on the Right argued that corruption was acceptable because it "greased the wheels" of international trade and capitalism and was therefore, at least within certain limits, a good thing. The World Bank and IMF, for example, and Western governments more generally, put institutional interests above all else, concluding that slinging mud at senior politicians in poor countries was no way to make friends and keep the Soviets at bay. Today, happily, the corruption portfolio transcends the old ideological divide. After being embraced at the World Bank by Wolfensohn and his left-liberal chief economist Joseph Stiglitz, it was also championed with gusto by Paul Wolfowitz from the opposite end of the policy spectrum, although not without serious institutional resistance.

Nonetheless, some echoes of past obstacles are still with us. Many non-governmental organizations see a focus on international financial flows and secrecy jurisdictions as a distraction from what they want: aid instead of better

[4]French Finance Minister Dominique Strauss-Kahn, in a speech to the Paris Group of Experts in March 1999, quoted in John Christensen and Mark Hampton, "All Good Things Come to an End", *The World Today* (August/September 1999). Use of tax havens has increased as a share of global trade since then.



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mobilization of domestic resources. At the same time, the old "corruption greases the wheels of business" argument lives on, as illustrated by a February 2007 *Economist* article that reported favorably on tax havens and the secrecy jurisdictions that host them. That being the case, it is not surprising that a modern equivalent of the FCPA such as the Financial Action Task Force, which ostensibly seeks to crack down on tax haven abuse, has failed to seriously dent the problem and, indeed, has helped legitimize the illegitimate.

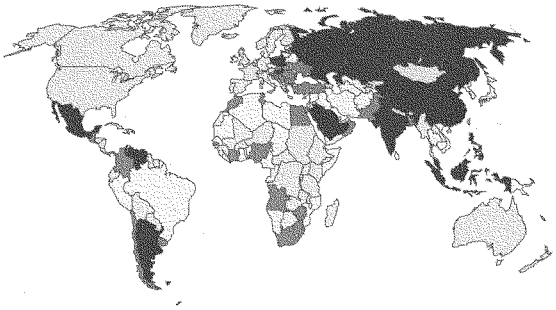
Nonetheless, change is afoot. Just as Watergate helped usher in a propitious climate for an anticorruption thrust in America in the 1970s, big changes now underway are likely to sustain and accelerate the shift toward a phase-two attack on corruption. Senator Barack Obama's backing for the Stop Tax Haven Abuse Act and an aggressive approach by the Internal Revenue Service against the Swiss banking giant UBS, which is suspected of facilitating tax evasion by wealthy Americans, are symptomatic of a changing political climate in the United States. Revelations in February that wealthy Europeans have been using accounts in Liechtenstein to evade taxes have contributed to a powerful mood shift against tax havens in Europe. In the past few months, OECD governments have also started discussing how they can cooperate on regulation and financial affairs. If the current subprime mess and evolving credit crunch are believed to be the leading edge of a deep, destabilizing global economic crisis, then we may expect greater resolve and cooperation in rectifying the huge imbalances in the global economy. That resolve will sooner or later transform the corruption debate, for there is no way to rectify the problem without addressing the corruption issue root and branch.

Of course, it won't be easy. Powerful vested interests have a lot to lose from cleaning up the current state of global capitalism. But the rest of us have even more to lose if we don't. If global capitalism cannot be rendered essentially fair, then it is unlikely to be sustainable in a world where formerly marginalized people are rapidly emerging from eons of political ignorance and passivity. We either join together to fix this problem, or it will surely "fix" us.

Illicit Financial Flows from Developing Countries: 2002—2006

Global Financial Integrity

Dev Kar and Devon Cartwright-Smith



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I. Introduction

1. Illicit financial flows generally involve the transfer of money earned through illegal activities such as corruption, transactions involving contraband goods, criminal activities, and efforts to shelter wealth from a country's tax authorities. However, such flows may also comprise funds that were earned through legitimate means. Thus defined, illicit flows involve funds that are illegally earned, transferred, or utilized and cover all *unrecorded* private financial outflows that drive the accumulation of foreign assets by residents in contravention of applicable laws and regulatory frameworks. In other words, if capital flows are unrecorded or if they skirt capital controls in place, such outflows are considered to be illicit for the purposes of this study. A uniform measure of illicit financial flows was adopted given that we are primarily interested in estimating the overall volume of such flows from developing countries and comparing them across various regions and countries. No attempt is made to differentiate the underlying activities that generate illicit financial flows.

2. This report is one of very few recent studies on the total volume and pattern of illicit financial flows out of all developing countries. Notably, the study by Raymond Baker used a survey-based approach to estimate illicit financial flows. His findings were later published in *Capitalism's Achilles Heel* (see Appendix II for full citation). Another comprehensive study, which is now somewhat dated, was carried out at the World Bank in 1994.

3. This study utilizes multiple economic models and filters to weed out spurious data in order to yield the most reliable estimates possible. However, it is important to note that all currently existing economic models have a limited capacity to reflect the actual volume of illicit financial flows, as these flows are primarily generated through transactions that completely bypass statistical recording. Because of this inability of official statistics to capture all of the monetary particulars of illegal commerce, which is the driving force behind these illicit outflows, the economic models used in this paper are likely to understate the true measure of illicit financial outflows from developing countries.

4. The list of 160 developing countries is based on the IMF's International Financial Statistics system of country classification, except for minor deviations that are noted. (See Appendix I for list and classification.)

II. Estimation Methods and Limitations

5. According to the models used in this paper, **illicit financial outflows occur through two channels—the clandestine use of the international banking system to send money out of a country, captured by the Hot Money (Narrow) and World Bank Residual models, and trade misinvoicing, which generates illicit funds that are shifted abroad.** Each of the three models used in this study—the Hot Money (Narrow), World Bank Residual, and Trade Misinvoicing—are widely used by economists. The data sources for this analysis are the large-scale macroeconomic databases maintained by the IMF and the World Bank. This study uses a "normalization" technique to weed out countries with low or spurious cases of illicit financial flows. The three models of illicit flows are briefly described below to illustrate how such flows are captured through the use of official data. In this paper, estimates of illicit financial flows from all developing countries are broken down into five regions of the world: Africa, Asia, Europe, Middle East and North Africa (MENA), and the Western Hemisphere.

6. **The Hot Money (Narrow) Model**: Estimates illicit financial flows by focusing strictly on the net errors and omissions line-item in a country's external accounts. The net errors and omissions figure balances credits and debits in a country's external accounts and reflects *unrecorded* capital flows and statistical errors in measurement. **A persistently large and negative net errors and omissions figure is interpreted as an indication of illicit financial outflows.**

7. **While the Hot Money (Narrow) method provides a measure of unrecorded capital flows in the balance of payments, the broadest version of the model, Hot Money 3, incorporates various recorded flows of short-term capital transactions carried out by the private sector.** Specifically, these include short-term private sector flows related to portfolio investments, equity securities, debt securities, money market instruments, trade credits, loans, currency and other deposits and investments. Consequently, if one were to focus exclusively on these recorded flows, such an exercise can yield estimates of licit financial flows from developing countries. However, estimates of licit financial flows are likely to be significantly understated because many developing countries do not report private short-term capital flows to the IMF. Keeping in mind these data limitations, we estimate that licit financial flows from developing countries (defined as those short-term private sector outflows recorded in the balance of payments) have more than doubled from $92.4 billion in 2002 to $207.6 billion in 2006 (see table below). Licit financial outflows from individual developing countries tend to be small, averaging less than 3 percent of GDP annually, although in a few cases they can average between 3-10 percent of GDP. Only in two cases, and mostly in response to significant political and macroeconomic instability, do such outflows rise to 10-12 percent of GDP in a particular year.

Licit Outflows ($millions)	2002	2003	2004	2005	2006
	$92,364	$67,141	$117,466	$175,856	$207,607

8. **The World Bank Residual Model**: Measures a country's source of funds (inflows of capital) against its recorded use (outflows and/or expenditures of capital). Source of funds includes increases in net external indebtedness of the public sector and the net inflow of foreign direct investment. Use of funds includes the current account deficit that is financed by the capital account flows and additions to central bank reserves. An excess source of funds over the recorded use (or expenditures) points to a loss of unaccounted-for capital and, as such, indicates illicit financial outflow.

9. This paper utilizes two alternative measures of net external indebtedness of the public sector: one based on annual **changes** in the stock of **external debt (CED)** and the other on the **net debt flows (NDF).** The inclusion of both the CED and NDF versions of the World Bank Residual model in this paper has to do with the impact of exchange rate valuation changes on the stock of debt. Valuation changes may overstate debt when the dollar is depreciating or understate debt when the dollar is appreciating vis-à-vis currencies in which the country had originally contracted the debt. Compared to the CED, the NDF version is generally preferred because exchange rate changes have a lower impact on the flows than on much higher stock figures. Since CED and NDF data should be consistent (except for differences in exchange valuation) we would not expect to see large differences in estimates of illicit financial flows estimates based on the CED and NDF data series which are independently compiled. This paper found that while illicit flows based on CED were higher than estimates based on NDF, the difference between them was only about 5 percent, on average, for the period 2002—2006.

10. **The Trade Misinvoicing Model:** Trade misinvoicing has long been recognized as a major conduit for illicit financial flows, the underlying motivation being that residents can illicitly acquire foreign assets by over-invoicing imports and under-invoicing exports. To estimate this kind of misinvoicing, a developing country's exports to the world are compared to what the world reports as having imported from that country, after adjusting for the cost of transportation and insurance. Additionally, a country's imports from the world are compared to what the world reports as having exported to that country. Discrepancies in partner-country trade data, after adjusting for the cost of freight and insurance, which imply over-invoicing of imports and/or under-invoicing of exports, indicates illicit flows. It should be noted however that the trade misinvoicing model can also yield a negative sign result, implying inward illicit flows (i.e. unrecorded capital flowing into a country) through export over-invoicing and import under-invoicing.

11. **This paper presents estimates of illicit financial flows based on two interpretations of the Trade Misinvoicing Model involving a netting method (Net) and a gross excluding reversals (GER) method.** In the Net method, gross capital outflows are reduced by gross capital inflows to derive a net position and only net positions with the correct (positive) sign are taken to represent illicit flows. In contrast, under the GER method, only estimates of export under-invoicing and import over-invoicing are included in the illicit flows analysis, while inward illicit flows (i.e., export over-invoicing and import under-invoicing) are ignored as they are deemed to result from spurious data. According to the GER method, the reduction of illicit financial outflows by inward illicit flows in the Net method is not realistic in countries with a history of poor governance and lack of prudent economic policies. As structural characteristics that drive illicit financial flows are unlikely to swing back and forth (particularly during a relatively short five-year period), the GER method limits inward illicit flows to clear cases where flight capital returns following genuine and sustained economic reform. Since it is hard to imagine legitimate traders using the trade misinvoicing mechanism to bring money into the country, the GER method is preferred in this paper.

12. It is worth bearing in mind that there are significant limitations to all three models for estimating illicit financial flows, not only because they cannot capture the many illegal channels for transferring money out of a country but also because the official data these models use are subject to errors in measurement. The following paragraphs (13-21) discuss some of these limitations.

13. The primary drawback of the Hot Money (Narrow) model is that the NEO not only reflects unrecorded capital flows but also statistical errors in recording a country's external transactions. In fact, in the case of many developing countries with weak balance of payments statistics, a significant part of the NEO may be due to statistical issues in recording the external accounts rather than a reflection of illicit financial flows. The other limitation of the Hot Money (Narrow) method arises from the fact that data on the NEO are missing for 31 countries (see Table 3) driving down the already low estimates of illicit flows. Of these countries, there are strong prima facie reasons to believe that illicit flows from Afghanistan, Algeria, Congo (DRC), Iran, Iraq, Somalia, and Uzbekistan could be significant due to economic and/or political instability. For these reasons, the Hot Money (Narrow) method provides significantly lower estimates of overall illicit flows from developing countries and is therefore not used to compare such flows between countries or analyze regional patterns and distributions.

14. Even if statistical problems in recording official data were nonexistent and we had full data coverage for all countries, none of the models economists use to estimate illicit financial flows can capture the effects of smuggling, as these types of transactions entirely bypass the customs authorities and their recording systems. Smuggling tends to be rampant when there are significant differences in cross-border prices in certain goods between countries that share a long and porous frontier. The profits from smuggling often end up as part of

outgoing illicit flows as smugglers seek to shield their ill-gotten gains from the scrutiny of officials, even as smuggling distorts the quality of bilateral trade. **As a result, trade data distortions due to smuggling may indicate that there are inward illicit flows into a country when in fact the reverse is true.**

15. The World Bank Residual model is subject to technical errors in accurately recording a country's external indebtedness, net foreign direct investments, and trade transactions (mainly related to goods and services). Also, the Bank seems to have more comprehensive data on the stock of external debt than on the net flows of new debt. In any case, the most reliable data series in the model would be the change in reserves, which is a figure typically compiled by the central bank and closely monitored in most developing countries.

16. Regarding limitations in the trade misinvoicing models, some economists have argued that misinvoicing should be excluded from estimates of illicit financial flows on the grounds that export under-invoicing and import over-invoicing behave quite differently from other conduits of illicit financial flows. For instance, misinvoicing often takes place in response to high trade taxes and thus may be unrelated to illicit financial flows captured by other models. However, other economists have advanced equally cogent arguments for including trade misinvoicing on the grounds that international trade often provides an excellent conduit for illicit financial flows. In their view, the exclusion of trade misinvoicing will seriously understate overall illicit flows. It is therefore not surprising that a number of recent studies sponsored by international organizations, such as the United Nations Conference on Trade and Development (UNCTAD), have explicitly included fake invoicing as a factor driving illicit financial flows. The UNCTAD study suggested that illicit financial outflows from Sub-Saharan Africa are fast approaching half a trillion dollars, more than twice the size of its aggregate external liabilities. Other country case studies on illicit financial flows such as Frank Gunter's (2003) on China or Prakash Loungani and Paolo Mauro's (IMF, April 2000) research on Russia explicitly include trade misinvoicing as a conduit for illicit flows. Schneider (2003) considered it startling to see the increase in capital lost through this channel in East Asia since the mid-1980s.

17. A further shortcoming in the comparison of partner-country trade statistics is that not all mispriced trade results in a difference between export and import values. When the misinvoicing occurs within the same invoice as a matter of agreement between buyer and seller there is no recorded difference between export and import values. This is the case in much of the abusive transfer pricing by multinational corporations, who vary invoices as needed to shift profits and capital across borders. In fact, transactions that are completely faked, without any underlying reality, have become common and are especially difficult to estimate. Asset swaps, yet another conduit for illicit flows, which are also difficult to estimate with confidence, have become common with Russian entrepreneurs, Latin American businesspeople, and Chinese state-owned enterprises. In fact, such swaps are increasingly used to shift assets out of developing countries and into Western economies.

18. As discussed above, there may be a complicated relationship between trade misinvoicing and illicit financial flows because misinvoicing may be driven by other motives to circumvent trade restrictions or to take advantage of government subsidies. For instance, if there are trade restrictions such as high import duties, imports may be under-invoiced to lower the burden of customs duties. A further complication may arise if one were to consider the rate of income taxation in relation to customs duties. If income taxes are higher than duties, an importer may still come out ahead by paying high customs duties (by over-invoicing imports) so long as the loss in income or profit results in lower income taxes that more than offset the higher customs duties.

19. The relationship between trade misinvoicing and illicit financial flows can also become very complicated if there are active black markets in foreign exchange operating within a country. For instance, if black market exchange rates are attractive, an importer may over-invoice imports to reduce taxable income and then reap the additional

profit from exchanging it in the black market. These illicit profits can then be transferred abroad through one or more of the conduits of illicit flows with which the importer is familiar. On the export side, illicit financial flows are common when the black market premium is higher than the export subsidy. It will then be attractive to raise the necessary foreign exchange on the black market.

20. Compounding the issues in tracking illicit financial flows listed above, there are statistical issues as well that detract from the accuracy of reported trade data. Differences in recording systems and the proper identification of the origin and destination of goods—particularly in an increasingly globalized world where component parts to a final product might originate from a number of countries—can complicate the identification and recording of an accurate country of origin for goods. Moreover, floating exchange rates can introduce exchange conversion-related discrepancies (because such conversion procedures are not uniform across all countries), given the long transit times involved in the exports and imports of certain heavy machinery or bulk container goods across the globe. It would be nearly impossible to distinguish discrepancies due to statistical issues in recording from those that arise as a result of deliberate misinvoicing. For this reason—in what represents a new and unique methodology and a departure from existing literature and studies— this study employs a normalization (see Charts 1 and 2) technique to filter out smaller discrepancies in partner-country trade data (amounting to less than 10 percent of exports) which could arise due to statistical issues and may not indicate illicit financial flows.

21. It must be noted that the World Bank Residual model considers the totality of financial, not value, flows. For example, if a country exports a good invoiced below the world market price, that transaction will reflect a financial, not a value, flow. The value flow will correspond to the difference in between the actual and the market value at local market prices. Illicit flows in terms of value will be streaming out of that country even if monetary funds are not. Hence, the World Bank Residual estimates, or those obtained through the Hot Money (Narrow) model, should be added to Trade Misinvoicing estimates in order to more accurately capture illicit flows.

III. Selection of Methods

22. Six combinations of economic models were tested in this study to select one that provides the most comprehensive and unbiased estimate. The six model combinations tested were:

Hot Money (Narrow)	+	Trade Misinvoicing (Net)
Hot Money (Narrow)	+	Trade Misinvoicing (GER)
World Bank Residual Model (CED)	+	Trade Misinvoicing (Net)
World Bank Residual Model (CED)	+	Trade Misinvoicing (GER)
World Bank Residual Model (NDF)	+	Trade Misinvoicing (Net)
World Bank Residual Model (NDF)	+	Trade Misinvoicing (GER)

23. A review of the methods used to estimate illicit financial flows shows that data limitations can seriously understate the volume of illicit financial flows from developing countries. In view of data limitations affecting the Hot Money (Narrow) model, this paper focuses on alternative versions of the World Bank Residual and the Trade Misinvoicing models to estimate the overall volume of illicit financial flows from developing countries.

24. As noted before, the World Bank Residual Model can be estimated using either the change in external debt (CED) or net flow of debt (NDF) as a source of financial resources for a country. However, while NDF data tend

to be less affected by valuation changes than the change in debt stocks, they are more likely to have gaps and be less-up-to-date compared to the CED data. These data issues may explain in general the somewhat lower illicit financial flows estimates based on NDF compared to those based on CED. The main limitation of the Net version of the Trade Misinvoicing model was that it gave undue credit to many developing countries for return of flight capital (that is an inflow of illicit capital) when in fact these countries did not implement a program of sustained economic reform that would be necessary to bring back such outflows. **Hence, while all of the models have been utilized in our analysis of illicit financial flows, the CED-GER combination of models was selected as the most reliable for studying the pattern of illicit flows from developing countries.**

IV. Process of Normalization

25. The previous discussion of the models used in this paper to estimate illicit financial flows has shown that some may significantly understate these flows. However, in arriving at a reliable estimate of illicit capital outflows, we must exercise care that such outflows are not overestimated either. The normalization process subjects the entire list of developing countries, for which data are available, to two filters: (i) estimates must have the right sign (indicating outflow, rather than inflow) in at least three out of the five years, and (ii) exceed the threshold (10 percent) with respect to exports valued at free-on-board (or f.o.b.) basis. Countries that pass through both filters are included in our estimates of illicit financial flows from the various regions of the developing world. The average and cumulative illicit flows for countries and regions exclude years when no such outflows are indicated. In contrast, the non-normalized method of deriving average and cumulative illicit flows for a country over the five-year period includes all cases where estimates had the right sign even for one year. In setting up this filter, the illicit financial flows-to-exports f.o.b. threshold ratio is set at 10 percent.

26. Under this normalization method, if model estimates indicate illicit financial flows out of a country in just two out of the five years (2002-2006), that country's estimates are rejected and we consider that there was no illicit financial flows from that country for the entire five-year period. Of the group of countries that have passed this filter, those with levels of illicit financial flows below the threshold stated above are rejected as reflecting data discrepancies due to statistical issues. This two-stage process of reducing the risk of including spurious cases of illicit financial flows is known as Normalization (see Charts 1 and 2).

27. **Non-normalized and normalized estimates of illicit financial flows represent the upper and lower bounds respectively of the possible range of illicit financial flows from developing countries generated by the combination of models presented in this paper.** Charts 1 and 2 show the filtration process for the GER and CED models.

28. Chart 1 (see next page) depicts the filtering process of GER data as a schematic diagram which illustrates how 43 countries were eliminated (117 remained) after the first filter and overall illicit financial flows dropped to an average of $399.1 billion per year. This group was then passed through the second filter, eliminating another 60 countries (i.e., only 57 countries made it through both filters) indicating that an average of $371.4 billion per year was shifted out of developing countries through trade misinvoicing during 2002---2006. Note that although the number of countries fell precipitously as they passed through the filters, the overall volume of illicit financial flows fell at a much lower rate. This is because the top 20 countries that account for the major share of illicit financial flows were caught by our illicit financial flows net, while the smaller exporters of capital fell through.

Chart 1. The Two-Stage Filtration Process for GER at 10 percent of Exports f.o.b.: A Schematic Diagram (Average 2002-2006)

All Developing Countries (See List in Appendix)

160 Countries
Est. Illicit Flows: $403.6 billion

Countries remaining after First Filter (Three Correct Signs)

Afghanistan, I.R. Of
Albania
Algeria
Angola
Argentina
Armenia
Aruba
Bahamas, The
Bangladesh
Barbados
Belarus
Belize
Benin
Bolivia
Bosnia & Herzegovina
Brazil
Brunei Darussalam
Bulgaria
Burkina Faso
Burundi
Cambodia
Cape Verde
Central African Rep.
Chad
Chile
China,P.R. Mainland
Colombia
Comoros
Congo, Dem. Rep. Of
Congo, Republic Of
Costa Rica
Croatia
Cyprus
Czech Republic
Djibouti
Dominica
Dominican Republic
Ecuador
Egypt
El Salvador
Equatorial Guinea
Ethiopia
Fiji
Gabon
Gambia, The
Georgia
Ghana
Grenada
Guatemala
Guinea
Guinea-Bissau
Honduras
India
Indonesia
Iran, I.R. Of
Jamaica
Kazakhstan
Kenya
Kuwait
Latvia
Lebanon
Liberia
Libya
Macedonia, Fyr
Madagascar
Malawi
Malaysia
Maldives
Mali
Malta
Mauritania
Mauritius
Mexico
Moldova
Morocco
Mozambique
Myanmar
Nepal
Nicaragua
Niger
Nigeria
Panama
Papua New Guinea
Paraguay
Peru
Philippines
Poland
Russia
Rwanda
Samoa
Seychelles
Sierra Leone
Slovak Republic
Solomon Islands
Somalia
South Africa
St. Kitts
St. Lucia
St. Vincent & Grens.
Sudan
Suriname
Syrian Arab Republic
Tajikistan
Tanzania
Thailand
Togo
Tonga
Trinidad & Tobago
Turkey
Turkmenistan
Uganda
Uruguay
Uzbekistan
Vanuatu
Venezuela, Rep. Bol.
Zambia
Zimbabwe

117 Countries
$399.1 billion

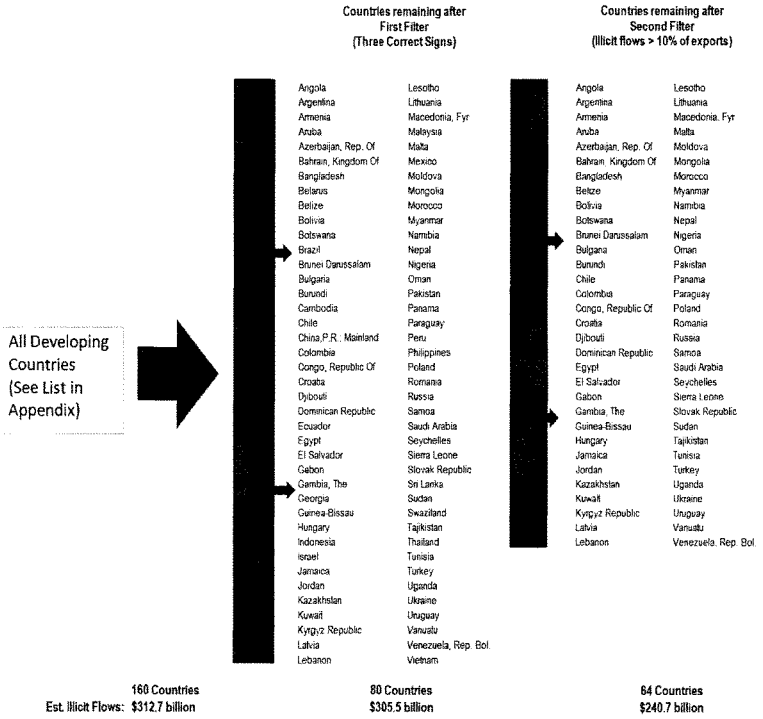
Countries remaining after Second Filter (Illicit Flows > 10% of exports)

Armenia
Aruba
Bahamas, The
Barbados
Belarus
Burkina Faso
Burundi
Cambodia
Cape Verde
Central African Rep.
China,P.R. Mainland
Comoros
Congo, Republic Of
Costa Rica
Cyprus
Djibouti
Egypt
El Salvador
Ethiopia
Gambia, The
Georgia
Grenada
Guatemala
Guinea
Guinea-Bissau
Honduras
India
Indonesia
Jamaica
Latvia
Macedonia, Fyr
Madagascar
Malaysia
Maldives
Mali
Malta
Mexico
Moldova
Mozambique
Nepal
Nicaragua
Panama
Paraguay
Philippines
Rwanda
Samoa
Seychelles
Sierra Leone
Solomon Islands
St. Kitts
St. Vincent & Grens
Syrian Arab Republic
Tajikistan
Togo
Vanuatu
Zambia
Zimbabwe

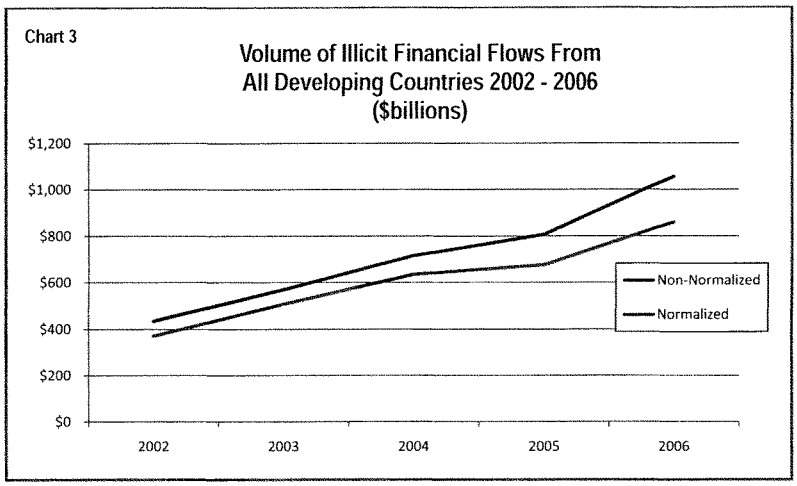
57 Countries
$371.4 billion

29. Chart 2 depicts a similar two-stage filtration process on average CED estimates of illicit financial flows. The two-stage filtration on CED indicates that on average $240.7 billion flowed out of developing countries per year over the same period. **Normalized estimates provided by the combined GER-CED models indicate that, on average, between $612.1 billion per year (normalized) and $716 (non-normalized) were shifted out of developing countries from 2002 to 2006.**

Chart 2. The Two-Stage Filtration Process for CED at 10 percent of Exports f.o.b.: A Schematic Diagram (Average 2002-2006)



V. Main Findings



30. In 2006, the last year for which official data are available, the range of illicit financial flows increased to between $858.6 billion (normalized)—$1.06 trillion dollars (non-normalized).

31. In 2002, the first year for which data were analyzed for this study, the volume of illicit financial flows from all developing countries ranged from $372.5 billion (normalized)—$435.4 billion (non-normalized).

32. The volume of illicit financial flows (normalized) from developing countries increased rapidly at an average rate of 18.2 percent per year over the period 2002 to 2006.

33. On average, illicit financial flows from all the developing countries ranged between $612 billion (normalized)—$716 billion (non-normalized) per year over the period 2002 to 2006.

34. The normalized and non-normalized estimates of illicit financial flows represent the lower and upper end of possible ranges presented in this study that can be compared to estimates obtained by previous researchers.

35. Charts 4 and 5 show estimated illicit financial flows during 2002—2006. The following observations can be made:

- While normalized and non-normalized numbers vary somewhat, illicit financial flows are increasing significantly regardless of the process of estimation.
- Illicit financial flows in the last year (2006) were more than double the volume of illicit financial flows at the beginning of the study (2002), regardless of whether estimates are normalized or not.

Chart 4 **Volume of Normalized Illicit Financial Flows From All Developing Countries: 2002 - 2006 ($billions)**

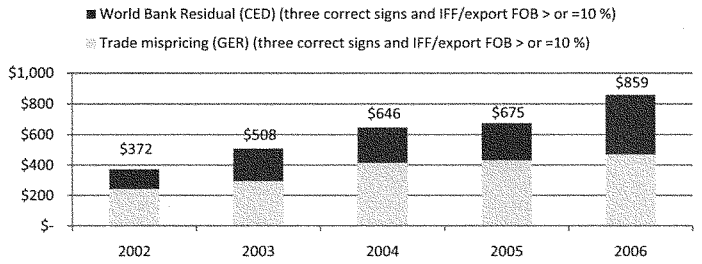
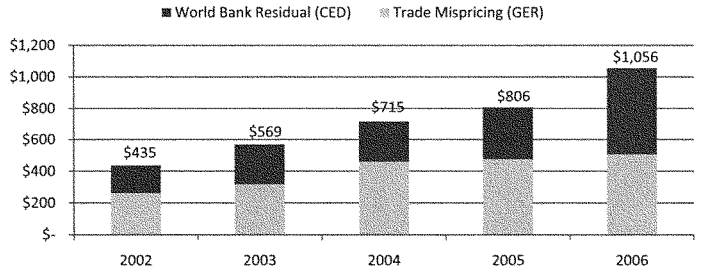


Chart 5 **Volume of Non-Normalized Illicit Financial Flows From All Developing Countries: 2002 - 2006 ($billions)**



36. Asia accounts for approximately 50 percent of overall illicit financial flows (Charts 6 and 7) from developing countries and normalization of the estimates does not significantly alter this picture. The large volume of illicit outflows from China (mainland) is behind Asia's dominance in overall illicit financial flows from developing countries.

37. About US$56 billion of nontrade illicit capital flowed about of China on average between 2002 and 2006. As this figure represents less than 10 percent of China's exports, this portion involving nontrade illicit flows was set to zero so that the entire illicit outflow from China estimated at US$233.5 billion results from trade mispricing. How does this estimate of illicit flows from China compare to recent estimates of capital flight by other researchers? Andong Zhu, Chunxiang Li, and Gerald Epstein (2005) present estimates of capital flight from China for the period 1982-2001 based on the World Bank residual method (using change in external debt) and adjusting these estimates for trade misinvoicing. According to their study, capital flight from China (excluding Hong-Kong) amounted to US$246.61 billion in 2000, which is slightly higher than the US$233.5 billion annual average for 2002-2006 estimated in this study.

38. A handful of countries in Europe, particularly Russia, are driving Europe's second place (around 16-17 percent) in the share of overall illicit flows from developing countries.

39. By far, the share of illicit flows from Africa is the lowest among all developing regions (approximately 3 percent of the total). **However, there are strong reasons to believe that the share would probably have been higher if more complete and reliable trade and external debt data were available (see chart 8 on next page).**

Average (2002-2006) Normalized Illicit Financial Flows from Developing Country Regions Based on CED-GER Models

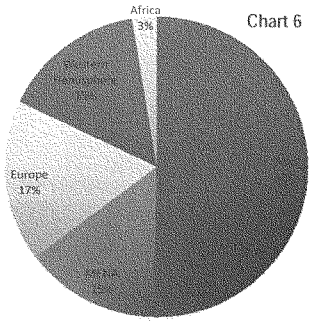


Chart 6

Average (2002-2006) Non-Normalized Illicit Financial Flows from Developing Country Regions Based on CED-GER Models

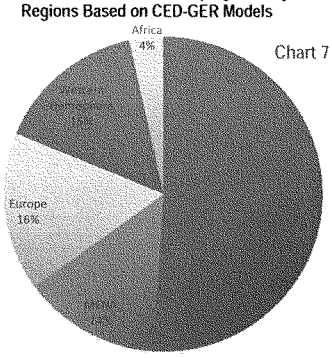
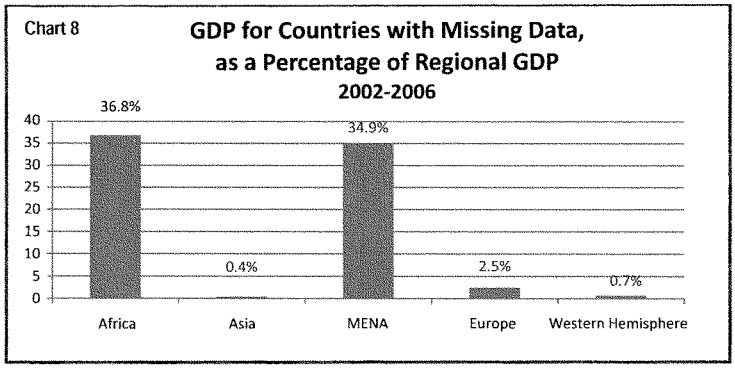


Chart 7



40. Chart 8 shows that countries in Africa with missing data have a cumulative GDP accounting for nearly 37 percent of total African GDP. Missing data, representing MENA countries accounting for nearly 35 percent of regional GDP, also understates illicit flows from that region. The chart shows that data gaps do not seriously understate illicit flows from Asia, Europe, or the Western Hemisphere. This measure assumes that the understatement of illicit flows varies directly with the size of the economy relative to the region. For example, missing data on Congo, Democratic Republic is likely to understate illicit flows from Africa to a much larger extent than missing data on Lesotho (i.e., the larger the economy the larger the potential illicit flows, other things being equal).

41. Given significant changes in the world economy such as the collapse of the Soviet Union, new states in Europe, and the rise of China, India and other emerging economies, the estimates obtained in this study can only be compared to the range obtained by Baker (2005) rather than those obtained in the dated World Bank (1994) study. This is the main reason why the normalized (low) and non-normalized (high) estimates obtained in this study are compared to range obtained by Baker in Chart 9.

42. Based on the survey method, Baker estimated that illicit financial flows from developing countries ranged from $539 to $778 billion in 2005 (referred to as the "Baker Range"). All models used in the present study were subjected to a process of Normalization; the CED-GER models yield a slightly higher range ($675 to $806 billion) of illicit financial flows in 2005. In the following year, model estimates indicate that illicit financial flows from developing countries increased to at least $858 billion and up to $1 trillion.

43. Chart 10 depicts the estimates of illicit financial flows obtained by this study for 2006, the most recent year for which data are available.

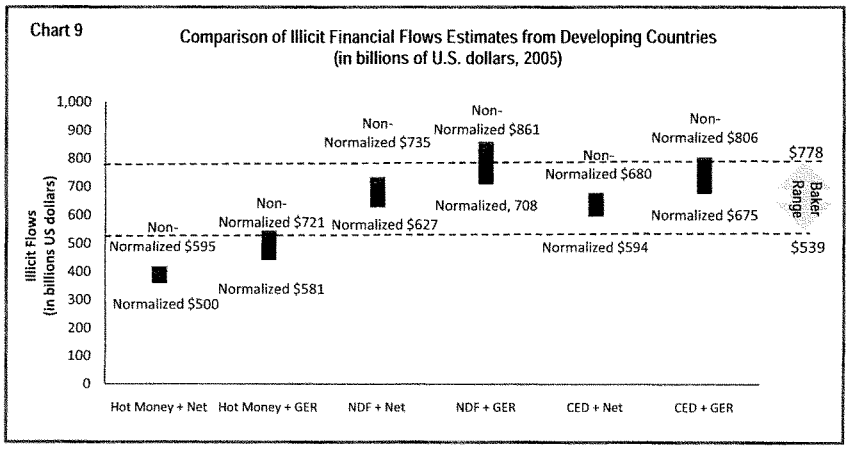


Chart 9
Comparison of Illicit Financial Flows Estimates from Developing Countries
(in billions of U.S. dollars, 2005)
Illicit Flows
(in billions US dollars)
1,000
900
800
700
600
500
400
300
200
100
0
Non-Normalized $595
Normalized $500
Non-Normalized $721
Normalized $581
Non-Normalized $735
Normalized $627
Non-Normalized $861
Normalized, 708
Non-Normalized $680
Normalized $594
Non-Normalized $806
Normalized $675
$778
$539
Baker Range
Hot Money + Net
Hot Money + GER
NDF + Net
NDF + GER
CED + Net
CED + GER

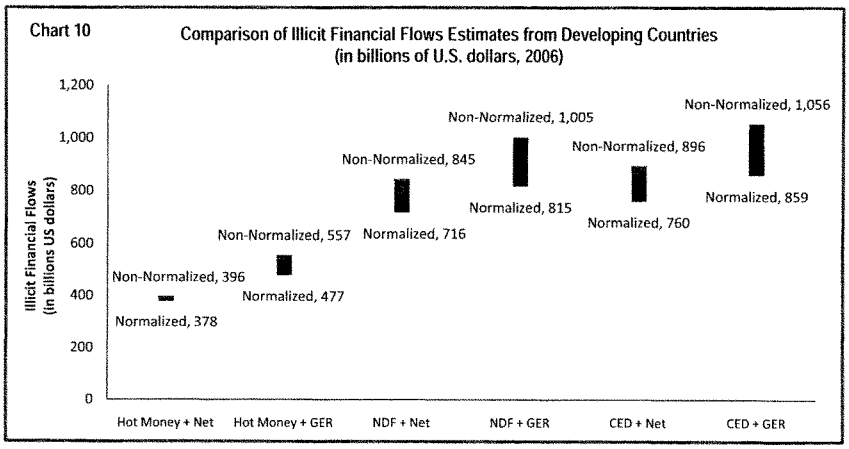


Chart 10
Comparison of Illicit Financial Flows Estimates from Developing Countries
(in billions of U.S. dollars, 2006)
Illicit Financial Flows
(in billions US dollars)
1,200
1,000
800
600
400
200
0
Non-Normalized, 396
Normalized, 378
Non-Normalized, 557
Normalized, 477
Non-Normalized, 845
Normalized, 716
Non-Normalized, 1,005
Normalized, 815
Non-Normalized, 896
Normalized, 760
Non-Normalized, 1,056
Normalized, 859
Hot Money + Net
Hot Money + GER
NDF + Net
NDF + GER
CED + Net
CED + GER

44. The regional dispersion of illicit financial flows discussed above is depicted in two full-page world maps that are color-coded to show the non-normalized and normalized global distribution of illicit financial flows as measured by the CED-GER models.

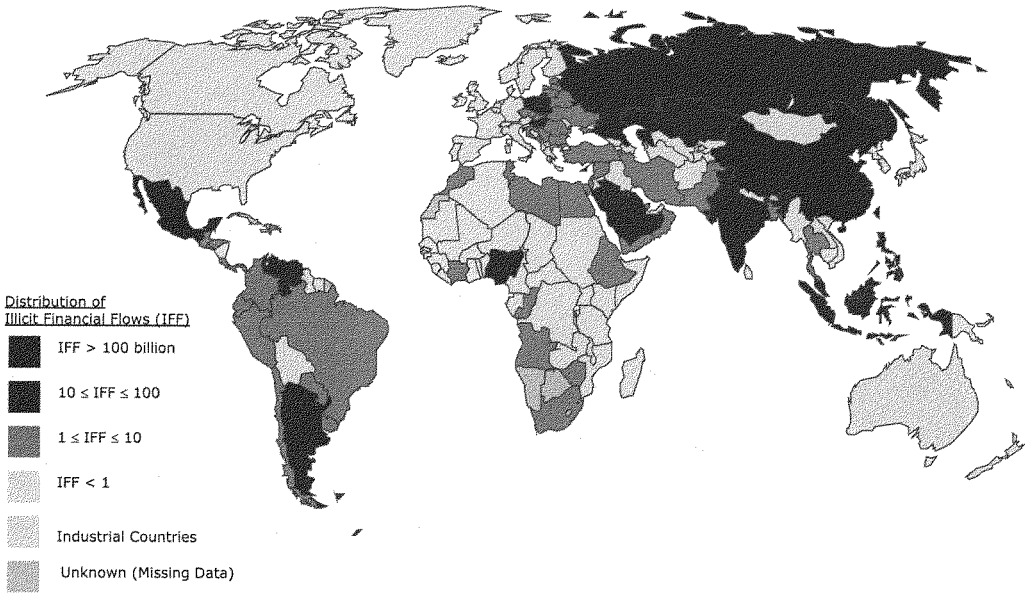
45. In these maps illicit financial flows from China stand out prominently as a hot spot (bright red), followed by countries in the greater than $10 billion but less than $100 billion category (dark red) which include Russia and India, while large swaths of the Western Hemisphere and parts of Africa fall in the greater than $1 billion but less than $10 billion category (orange). A large part of Africa shows illicit flows of less than $1 billion dollars annually (yellow). This global distribution of illicit flows remains basically intact upon normalization (World Map 2), except that countries with less than $10 billion in illicit flows involving large parts of the Western Hemisphere and Africa now fall below the threshold imposed by normalization (light blue).

46. Over the five-year period of the study, illicit financial flows grew at the fastest pace in the MENA region, followed by Europe, Asia, Africa, and the Western Hemisphere in that order. This pattern of growth in illicit flows remains invariant with respect to the normalization process. The nearly 50 percent compound rate of growth in illicit flows from the MENA region simply reflects the phenomenal growth of CED components such as the current account surplus and external debt of many oil producing countries in that region. This study's finding of a sharp increase in illicit flows from the MENA region is consistent with a study by Abdullah Almounsor (2005), who found that illicit financial flows from Saudi Arabia increased by approximately 900 percent in 1974 following the first oil shock and noted the significance of natural resource rents, especially crude oil rents, in contributing to capital flight from resource-rich states.

47. In the normalized and non-normalized top-ten lists of countries with the highest volumes of illicit financial flows, **eight out of the ten countries—China, Saudi Arabia, Mexico, Russia, Malaysia, India, Kuwait, and Venezuela**—are not affected by the normalization process and are therefore in both lists. Indonesia and the Philippines are in the non-normalized list while Hungary and Poland are on the normalized side.

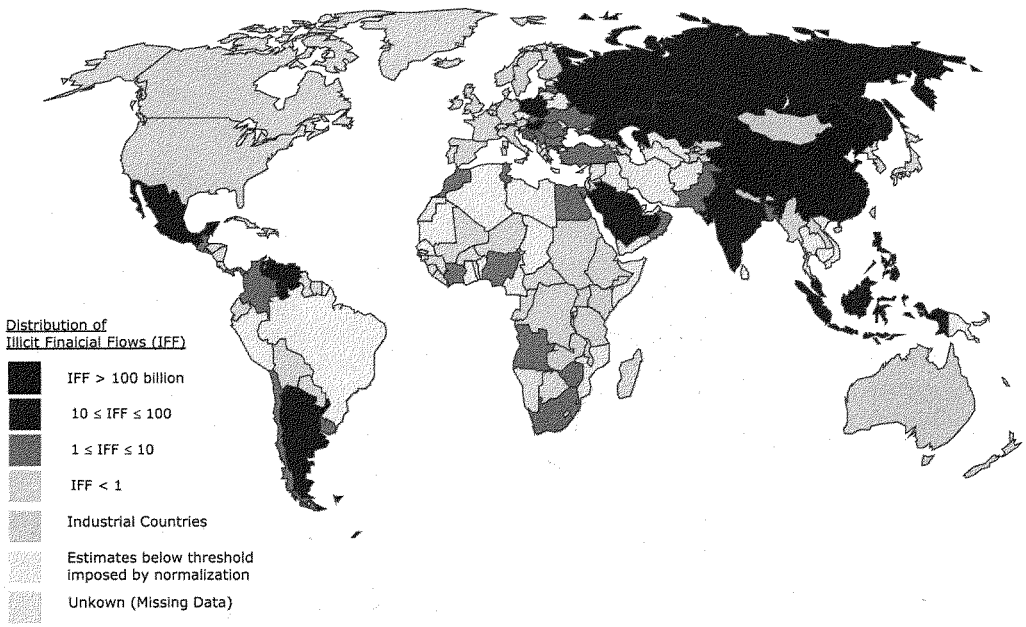
48. Six of the top ten countries with the highest average illicit financial flows during 2002—2006 (Indonesia, Kuwait, Mexico, Russia, Saudi Arabia, and Venezuela) are oil exporters (see Charts 11 and 12); Indonesia does not make the cut if estimates are normalized.

Chart 11 Global Distribution of Non-normalized Illicit Financial Flows, Average 2002-06[1]



[1] Serious data issues prevented separate estimation of illicit financial flows out of Hong Kong and Macau.

Chart 12 Global Distribution of Normalized Illicit Financial Flows, Average 2002-06[1]



[1] Serious data issues prevented separate estimation of illicit financial flows out of Hong Kong and Macau.

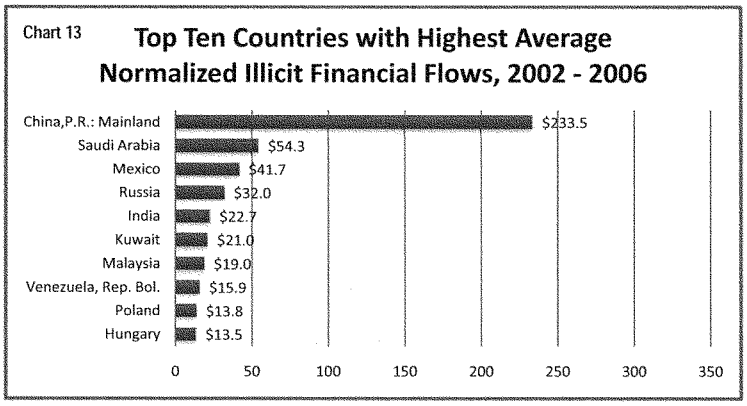


Chart 13
Top Ten Countries with Highest Average Normalized Illicit Financial Flows, 2002 - 2006
China,P.R.: Mainland
Saudi Arabia
Mexico
Russia
India
Kuwait
Malaysia
Venezuela, Rep. Bol.
Poland
Hungary
$233.5
$54.3
$41.7
$32.0
$22.7
$21.0
$19.0
$15.9
$13.8
$13.5
0
50
100
150
200
250
300
350

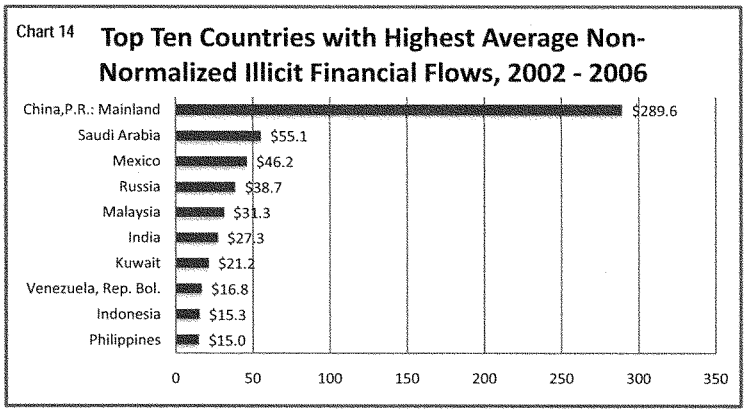


Chart 14
Top Ten Countries with Highest Average Non-Normalized Illicit Financial Flows, 2002 - 2006
China,P.R.: Mainland
Saudi Arabia
Mexico
Russia
Malaysia
India
Kuwait
Venezuela, Rep. Bol.
Indonesia
Philippines
$289.6
$55.1
$46.2
$38.7
$31.3
$27.3
$21.2
$16.8
$15.3
$15.0
0
50
100
150
200
250
300
350

VI. Summary of Findings and Conclusions

49. Out of the models for estimating illicit financial flows reviewed in this study, the World Bank Residual model combined with the Trade Mispricing model provided the most unbiased and robust estimates of illicit financial flows (as data limitations were minimal).

50. Illicit financial flows driven by illicit activities are growing at a rapid and steady pace, draining poor countries of billions of dollars every year.

51. In a regional breakdown, this study found that developing Asia accounts for around half of the overall illicit flows from developing countries. The disproportionate volume of illicit flows from mainland China led Asia to dominate in overall illicit flows from developing countries and makes a strong case for future research to carry out an in-depth analysis of the factors driving such outflow from mainland China.

52. A handful of countries in Europe, including Russia, put Europe in second place (around 16-17 percent) in the share of overall illicit flows from developing countries. Again, a separate study is warranted given the paucity of in-depth research on illicit flows from Russia following the recent dramatic surge in crude oil prices. Average normalized illicit flows from Western Hemisphere (at 15.2 percent of the average for all developing countries) are slightly more than the average illicit capital outflows from the MENA region (at 14.8 percent). By far, the share of illicit flows from Africa is the lowest among all developing regions (approximately 3 percent of the total). However, there are strong reasons to believe that the share of Africa in total illicit flows would probably be higher if more complete and reliable external debt data were available.

53. Over the period 2002-2006, illicit financial flows grew at the fastest pace in the MENA region, followed by Europe, Asia, Africa, and the Western Hemisphere, in that order. This pattern of growth in illicit flows remains invariant with respect to the normalization process. The nearly 50 percent compound rate of growth in illicit flows from the MENA region reflects the exponential growth of CED components such as the current account surplus and external debt of many oil producing countries in that region. At the same time, GER registers a low figure because as noted earlier, oil trade presents somewhat constrained opportunities for trade mispricing. Europe registers a compound annual rate of growth in illicit flows of nearly 25 percent (whether estimates are normalized or not) mainly reflecting the huge and growing outflows from Russia.

54. Due to the fact that official statistics cannot fully capture the volume of illicit financial flows from developing countries, estimates of these flows based on existing economic models are likely to understate the actual problem. Hence, normalized estimates of illicit flows from developing countries and regions are likely to be extremely conservative.

A longer version of this report, also authored by Lead Economist Dev Kar and Research Associate Devon Cartwright-Smith, includes technical subject matter, additional details about the models utilized and a full statistical appendix. This version is likely to be of interest to economists.

The Statistical Appendix in the longer version of the report includes 20 tables. The first three show the nature and extent of capital controls in developing countries, the system of classifying developing countries, and the extent of data deficiencies affecting the Hot Money (Narrow) model. The remaining tables provide alternative estimates of illicit financial flows through trade misinvoicing and the summary estimates of non-normalized and normalized illicit financial flows provided by the various models and the regional breakdown of these estimates. Two tables show the non-normalized and normalized estimates of illicit outflows for individual countries obtained by applying the CED-GER models. The final table lists the 28 countries and the volume of illicit flows which were eliminated through the normalization procedures.

Both versions of this report are available for download at www.gfip.org.

Global Financial Integrity (GFI) promotes national and multilateral policies, safeguards, and agreements aimed at curtailing the cross-border flow of illegal money. In putting forward solutions, facilitating strategic partnerships, and conducting groundbreaking research, GFI is leading the way in efforts to curtail illicit financial flows and enhance global development and security.

Appendices

Appendix I: List of 160 Developing Countries

Africa - 48	Asia - 30	Europe – 31	Middle East and North Africa - 18	Western Hemisphere - 33
Angola	Afghanistan, I. R. of	Albania	Algeria	Antigua & Barbuda
Benin	Bangladesh	Armenia	Bahrain, Kingdom of	Argentina
Botswana	Bhutan	Azerbaijan, Rep. of	Egypt	Aruba
Burkina Faso	Brunei Darussalam	Belarus	Iran, I. R. of	Bahamas, The
Burundi	Cambodia	Bosnia & Herzegovina	Iraq	Barbados
Cameroon	China, R. : Mainland	Bulgaria	Israel	Belize
Cape Verde	Fiji	Croatia	Jordan	Bolivia
Central African Rep.	India	Cyprus	Kuwait	Brazil
Chad	Indonesia	Czech Republic	Lebanon	Chile
Comoros	Kiribati	Estonia	Libya	Colombia
Congo, Dem. Rep. of	Lao People's Dem. Rep	Georgia	Morocco	Costa Rica
Congo, Republic of	Malaysia	Hungary	Oman	Dominica
Côte D'Ivoire	Maldives	Kazakhstan	Qatar	Dominican Republic
Djibouti	Marshall Islands	Kyrgyz Republic	Saudi Arabia	Ecuador
Equatorial Guinea	Micronesia	Latvia	Syrian Arab Republic	El Salvador
Eritrea	Mongolia	Lithuania	Tunisia	Grenada
Ethiopia	Myanmar	Macedonia, FYR	United Arab Emirates	Guatemala
Gabon	Nepal	Malta	Yemen, Republic of	Guyana
Gambia, The	Pakistan	Moldova		Haiti
Ghana	Palau	Montenegro		Honduras
Guinea	Papua New Guinea	Poland		Jamaica
Guinea-Bissau	Philippines	Romania		Mexico
Kenya	Samoa	Russia		Nicaragua
Lesotho	Solomon Islands	Serbia		Panama
Liberia	Sri Lanka	Slovak Republic		Paraguay
Madagascar	Thailand	Slovenia		Peru
Malawi	Timor-Leste	Tajikistan		St. Kitts
Mali	Tonga	Turkey		St. Lucia
Mauritania	Vanuatu	Turkmenistan		St. Vincent & Grenadines
Mauritius	Vietnam	Ukraine		Suriname
Mozambique		Uzbekistan		Trinidad & Tobago
Namibia				Uruguay
Niger				Venezuela, Rep. Bol.
Nigeria				
Rwanda				
São Tomé & Principe				
Senegal				
Seychelles				
Sierra Leone				
Somalia				
South Africa				
Sudan				
Swaziland				
Tanzania				
Togo				
Uganda				
Zambia				
Zimbabwe				

The country classification used in this study differs from the IMF's International Financial Statistics (IFS) as follows: (i) Korea and Singapore are excluded, as they are considered to be industrial countries and (ii) North Africa (Algeria, Morocco, Tunisia) are classified under the group Middle East and North Africa (MENA), rather than Africa, as in IFS.

Appendix II. Normalized and Non-Normalized Country Rankings

Yearly Average Illicit Financial Outflows
Normalized and Non-Normalized 2002-2006, values in US$ millions

Country	Normalized	Rank	Non-Normalized	Rank
China,P.R.: Mainland	233,520	1	289,552	1
Saudi Arabia	54,258	2	55,147	2
Mexico	41,680	3	46,156	3
Russia	32,025	4	38,688	4
Malaysia	19,027	7	31,271	5
India	22,726	5	27,304	6
Kuwait	21,040	6	21,208	7
Venezuela, Rep. Bol.	15,896	8	16,802	8
Indonesia	10,361	14	15,345	9
Philippines	12,154	11	15,048	10
Poland	13,762	9	14,066	11
Hungary	13,460	10	13,460	12
Argentina	12,099	12	13,040	13
Nigeria	9,112	16	12,513	14
Kazakhstan	11,734	13	12,098	15
Turkey	9,546	15	11,075	16
Ukraine	8,519	17	8,547	17
Brazil	0	...	8,407	18
Chile	6,961	19	8,173	19
Czech Republic	0	...	7,834	20
Belarus	7,217	18	7,686	21
Qatar	0	...	6,863	22
Egypt	6,836	20	6,836	23
South Africa	0	...	6,445	24
Thailand	0	...	6,302	25
Croatia	5,149	21	5,354	26
Syrian Arab Republic	2,956	27	4,226	27
Panama	4,070	22	4,070	28
Colombia	2,559	30	3,855	29
Romania	3,836	23	3,836	30
Slovak Republic	2,994	26	3,520	31
Costa Rica	3,229	25	3,323	32
Brunei Darussalam	3,299	24	3,305	33
Libya	0	...	3,199	34
Morocco	2,109	34	3,093	35
Pakistan	2,358	33	3,067	36
Israel	0	...	3,023	37
Azerbaijan, Rep. Of	640	58	2,834	38
Latvia	2,822	28	2,822	39
Angola	2,730	29	2,764	40

Yearly Average Illicit Financial Outflows

Normalized and Non-Normalized 2002-2006, values in US$ millions

Country	Normalized	Rank	Non-Normalized	Rank
Uruguay	2,407	32	2,620	41
Bulgaria	1,974	36	2,492	42
Aruba	2,469	31	2,469	43
Bangladesh	1,689	40	2,344	44
Peru	0	...	2,227	45
Lebanon	1,953	37	2,111	46
Congo, Republic Of	2,060	35	2,060	47
Honduras	1,674	41	1,858	48
Oman	1,602	42	1,826	49
Dominican Republic	1,816	38	1,821	50
Tunisia	1,727	39	1,727	51
Bahrain, Kingdom Of	1,512	43	1,512	52
Lithuania	1,457	44	1,457	53
Ecuador	0	...	1,368	54
Ethiopia	423	67	1,333	55
El Salvador	1,292	45	1,292	56
Guatemala	1,187	46	1,187	57
Gabon	996	48	1,031	58
Malta	1,014	47	1,014	59
Zambia	678	57	986	60
Cyprus	766	52	980	61
Bolivia	787	51	898	62
Vietnam	0	...	876	63
Paraguay	857	49	857	64
Cameroon	0	...	842	65
Jamaica	840	50	840	66
Sudan	740	54	830	67
Jordan	577	63	751	68
Zimbabwe	750	53	750	69
Yemen, Republic Of	0	...	740	70
Nicaragua	723	55	723	71
Namibia	688	56	688	72
Kenya	0	...	686	73
Tanzania	0	...	660	74
Mali	573	64	629	75
Myanmar	624	59	628	76
Estonia	0	...	610	77
Mozambique	207	77	604	78
Nepal	600	60	600	79
Botswana	597	61	597	80
Maldives	593	62	593	81
Georgia	472	65	527	82
Ghana	0	...	482	83
Macedonia, Fyr	457	66	457	84
Cambodia	382	69	457	85
Guinea	363	70	430	86

Yearly Average Illicit Financial Outflows
Normalized and Non-Normalized 2002-2006, values in US$ millions

Country	Normalized	Rank	Non-Normalized	Rank
Turkmenistan	0	...	429	87
Mauritius	0	...	414	88
Mongolia	224	75	398	89
Armenia	397	68	397	90
Sri Lanka	0	...	358	91
Slovenia	0	...	356	92
Moldova	345	71	345	93
Madagascar	226	74	326	94
Barbados	307	72	307	95
Tajikistan	277	73	277	96
Papua New Guinea	0	...	270	97
Trinidad & Tobago	0	...	225	98
Uganda	178	80	217	99
Samoa	216	76	216	100
Algeria	0	...	203	101
Seychelles	192	78	192	102
St. Vincent & Grens.	180	79	190	103
Togo	118	82	167	104
Rwanda	105	85	167	105
Benin	0	...	163	106
Swaziland	0	...	156	107
Iran, I.R. Of	0	...	145	108
Djibouti	119	81	119	109
Bahamas, The	117	83	117	110
Burundi	110	84	110	111
Lesotho	105	86	105	112
Mauritania	0	...	102	113
Kyrgyz Republic	86	88	101	114
Niger	0	...	101	115
Haiti	0	...	98	116
Fiji	0	...	94	117
Sierra Leone	92	87	92	118
Senegal	0	...	88	119
Albania	0	...	76	120
Bosnia & Herzegovina	0	...	71	121
Cape Verde	18	96	70	122
Somalia	0	...	63	123
Liberia	0	...	63	124
Burkina Faso	57	89	57	125
Gambia, The	56	90	56	126
Central African Rep.	51	91	51	127
Solomon Islands	21	95	49	128
Grenada	26	94	47	129
Dominica	0	...	36	130
Belize	34	92	35	131
Guyana	0	...	35	132

Yearly Average Illicit Financial Outflows
Normalized and Non-Normalized 2002-2006, values in US$ millions

Country	Normalized	Rank	Non-Normalized	Rank
Guinea-Bissau	27	93	27	133
Vanuatu	12	97	12	134
St. Lucia	0	...	7	135
Suriname	0	...	5	136
Malawi	0	...	5	137
Congo, Dem. Rep. Of	0	...	5	138
Equatorial Guinea	0	...	4	139
St. Kitts	4	98	4	140
Afghanistan, I.R. Of	0	...	3	141
Comoros	3	99	3	142
Iraq	0	...	2	143
Tonga	0	...	1	144

Country estimates that are zero or have data issues are not listed in this table.

Source: Direction of Trade Statistics, Balance of Payments, International Finance Statistics databases of the IMF, as well as Global Development Finance database of the World Bank

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Appendix IV: Biographies

DR. DEV KAR
Lead Economist, Study Author

Dev Kar is a Lead Economist at the Global Financial Integrity Program, Center for International Policy. Prior to joining CIP, Dr. Kar was a Senior Economist at the International Monetary Fund (IMF), Washington DC. During a career spanning nearly 32 years at the IMF, he worked on a wide variety of macroeconomic and statistical issues, both at IMF headquarters and on different types of IMF missions to member countries (technical assistance, Article IV Consultations with member countries, and Use of IMF Resources).

Dr. Kar's assignments at the IMF included: (i) research studies on the functions and role of central banks which formed the basis for the design, development, and implementation of a large-scale database on laws, regulations, and data on various aspects of central banking operations, (ii) technical papers on the operational budget of the IMF, (iii) carrying out complex IMF operational transactions with member countries, (iv) review of IMF lending programs involving the use of its financial resources in order to assess sovereign and liquidity risks, (v) the monitoring of economic and political developments in Heavily Indebted Poor Countries (HIPC) and in Poverty Reduction and Growth Facility (PRGF)-eligible countries, (vi) preparation of research papers and discussion notes on the role of the SDR in the international monetary system and the use of the SDR as a unit of account by multilateral institutions, (vii) critiquing technical assistance papers based on expert technical knowledge of international methodological guidelines on national accounts, price statistics, and merchandise trade, (viii) providing technical assistance to member countries in the area of national accounts, prices, and external trade in order to build members' statistical capacities, (ix) preparing papers for discussion by the IMF Executive Board on recent cases of overdue financial obligations of certain members and assessing the likelihood of payments by these countries, (x) preparing short papers on the external debt situation of heavily indebted countries and providing technical assistance to IMF economists in forecasting external debt profiles, (xi) conducting extensive research on early warning models that seek to predict an external debt crisis for heavily indebted countries, and (xii) developing statistical measures and indicators on quantitative and non-quantitative trade restrictions, dumping, and other trade policy issues, comparing them across countries and within countries over time. Dr. Kar has a Ph.D. in Economics from the George Washington University (Major: Monetary Economics), an M. Phil (Economics), also from the same university (Major: International Economics) and a M.S. (Computer Science) from Howard University (Major: Database Management Systems). He obtained an undergraduate degree in Physics from St. Xavier's College, University of Calcutta, India. Dev has published a number of articles on macroeconomic and statistical issues both inside and outside the IMF.

DEVON CARTWRIGHT-SMITH
Senior Research Associate, Study Co-Author

Devon Cartwright-Smith is the Senior Research Associate at Global Financial Integrity. He is also currently in the Doctoral Program in Economics at Georgetown University. Prior to joining GFI, Mr. Cartwright-Smith was the Operations Analyst at Baker & Taylor, the largest U.S. distributor of books, music and movies for libraries and retailers, with six branches nationwide. While there, he reengineered the previous approach to data collection and processing into vastly more efficient methods. He moved the company from a manual reporting framework to a fully automated Excel-driven reporting system. He was regularly sought out by several other departments, company-wide, to develop creative solutions to problems and operational inefficiencies.

Mr. Cartwright-Smith graduated from Bates College in 2003 with a degree in Economics. For his senior thesis, he acquired data from over 1100 completed eBay auctions using original scripts written in Excel, defined new market spaces for item types, and created and parameterized a pair of models, one for each market space, that determined, in a linear regression analysis, the final price in an auction and, alternatively, the number of bidders in an auction. In 2001 he won a competitive fellowship, where he was retained as a consultant to advise the city of Lewiston, Maine on strategies for implementing a mixed-income housing initiative.

RAYMOND W. BAKER
Director, Global Financial Integrity

Raymond Baker is an internationally respected authority on corruption, money laundering, growth and foreign policy issues in developing and transitional economies and the impact of these problems on western economic and foreign interests. He has written and spoken extensively, testified before U.S. Senate and House committees and U.K. Parliamentary committees, been quoted worldwide, and has commented frequently on television and radio in the United States, Europe and Asia on legislative matters and policy questions, including appearances on Nightline, CNN, BBC, NPR, ABC, Four Corners in Australia and Fifth Estate in Canada, among others. He is the author of ***Capitalism's Achilles Heel: Dirty Money and How to Renew the Free-Market System*** (John Wiley & Sons), recognized by the *Financial Times* as one of the best business books of 2005

Mr. Baker is a Guest Scholar at the Brookings Institution and a Senior Fellow at the Center for International Policy where he directs the **Global Financial Integrity (GFI)** program.

Testimony of Jack A. Blum, Esq.

Before the Committee on Financial Services, U.S. House of Representatives

May, 19, 2009

The problem of Curbing Grand Scale Global Corruption

My name is Jack Blum. I am a Washington lawyer who works on issues related to international corruption, tax evasion and financial crime. My practice focuses includes money laundering compliance work for banks and brokerage firms, representation of the victims of complex financial fraud, and assistance to various governments and government agencies regarding offshore financial structures and tax evasion. I currently represent the Government of Nigeria in its efforts to obtain mutual legal assistance from the United States in the KBR bribery case - a case that illustrates the problems of dealing with cross border corruption and about which I will say more about in my testimony.

Thirty years of experience with foreign corruption issues has led me to the following conclusions:

- Amendments to the Foreign Corrupt Practices Act (FCPA) may facilitate domestic prosecutions, but will not address the major underlying issue - grand scale corruption which impoverishes a nation to enrich the people who run the government.
- Years of work on mutual legal assistance treaties and anti-corruption conventions designed to facilitate cooperation have still not made the prospect of bringing all of the perpetrators of grand scale corruption to justice more likely. Nothing addresses corruption in plain sight -- the agreements are all designed to respond after the fact.
- The best prospect for real results lie in the area of civil recovery undertaken by itself or in conjunction with criminal prosecution.
- To help the effort Congress should pass laws facilitating civil recovery, laws that expand the jurisdiction of US courts on these matters and that hold financial institutions civilly liable for failure to protect the interests of the beneficial owners of stolen money -- the country that was looted.

The grand scale corruption issue is more important than ever. Obvious cases of grand scale corruption abound. Examples include the Obiangs of Equatorial Guinea, the family of the president of Kazakhstan, the now retired Daniel Arap Moi of Kenya, and the former presidents of Nigeria who retired to London with a substantial portion of the national patrimony. The amounts flowing out of the developing world as a result of corruption in all probability exceed the amount of direct foreign assistance flowing in. Finding a way of curbing the flow of this corruption money must be a priority.

The existing network of treaties and conventions, while far better than the one in place thirty years ago, is still not effective in stopping the flow of illicit funds. The problems are deep and systemic and require careful thought. At the core is the same central problem at the heart of every truly global issue in urgent need of solution -- the prerogatives of national sovereignty. In no area are those prerogatives more

vigorously asserted than in the area of criminal law -- and anti-corruption efforts have mostly focused on criminal law responses.

The need for global coordination on the issue of corruption was obvious when the FCPA was being considered. In the 1970's the Senate Foreign Relations Committee, which I then served as Associate Counsel, exposed the bribes Lockheed Aircraft paid to a clutch of foreign heads of state including the Prime Minister of Japan. At the time, there was no mechanism for the Senate to share its evidence with the Japanese prosecutors or for that matter with the prosecutors of other interested countries. The State Department then began urgent negotiations with Japan which put in place the first mutual legal assistance agreement. Others quickly followed.

What the countries did with the evidence was up to them. Japan eventually prosecuted, convicted and imprisoned Prime Minister Tanaka. In contrast, Mexico never even requested the Lockheed evidence the Foreign Relations Committee had obtained.

Working for the UN Centre on Transnational Corporations in 1976 I attempted to draft an international anti-corruption agreement. That first UN effort was, and still is, referred to in some quarters as the "disaster of 1976." Ideological differences, commercial rivalries, and national interests overrode what little momentum the anti-corruption initiative had. I learned that nothing could be drafted that would in any way interfere with national sovereignty. In plain English if the crook is a sitting head of state there is nothing the international community can do short of an embargo or invasion.

I revisited the corruption issue in the late 1980's as Special Counsel to the Senate Foreign Relations Committee - this time as the Committee began to look into the issue of money laundering. I vividly remember a drug dealer who had roots in the Cayman Islands testifying, almost as an aside, that the then Prime Minister of Jamaica, Edward Seaga, had hidden bank accounts in Cayman. When the hearing ended, and I returned to my office my phone rang with a call from a very angry Prime Minister Seaga. He wanted to know how he was to handle a situation in which he could not defend himself.

"What business was it of the United States to undermine this government?," he asked. "How can I possibly defend myself? Was this not an attack on Jamaican sovereignty?"

Indeed the questions had merit and were part of the same challenge the Committee faced in the Lockheed Japanese bribery case. How could the United States open an investigation that would lead to corruption charges against a foreign head of state who could not be prosecuted here? What were the foreign policy implications?

In 1989 I was the co-author of a UN Report on Offshore Havens and Money Laundering and in 1990 became the Chair of a UN Experts group on asset recovery. Our objective was to find a way for counties which had been victimized by grand scale corruption to go after the funds using civil actions and repatriate them.

The experts group included lawyers and persecutors from around the world. In the course of our wide ranging discussions the limits of criminal prosecution became apparent. Criminal law by its very nature is

territorial. Countries can prosecute crimes within their jurisdiction. In some cases countries expand their jurisdictional claims to cover crimes against their citizens, crimes by their citizens wherever committed, and crimes that have an impact on their territory. To deal with the issue of crimes that cross borders, countries have developed a system of extradition treaties and mutual legal assistance agreements. Thus far, with the exception of the International Criminal Court which the United States does not participate in, there is no international criminal law. Indeed, the newly negotiated anti-corruption conventions still call signatory state to pass their own implementing criminal legislation.

There are many good reasons to be cautious when it comes to the creation of an international criminal law. For the United States the most serious is the preservation of the Constitutional rights of American citizens. While our system of justice has its flaws most of us would find it unacceptable to be charged in a system that lacked the Fifth Amendment right to remain silent, did not guarantee a jury trial or did not presume innocence until proven guilty.

As a result of the territorial limitations, criminal law is largely dysfunctional in the area of complex white collar crime. Despite the plethora of bi-lateral mutual legal assistance agreements it is still virtually impossible to compel testimony in a US court from a foreign witness who chooses not to cooperate. Although there are procedures for the movement of evidence across international borders, the process is slow and cumbersome. National interests and political forces sometime trump real cooperation. A screaming example of this is the BAE (British Aircraft Industries) Saudi bribery case which was closed down by the UK government. The UK was shameless in saying the investigation was closed to protect the thousands of jobs tied to the global defense equipment contracts the company had obtained. My understanding is that the Justice Department is pursuing the case, but without the active help of the UK I do not expect much.

Then there is the issue of corruption in Kazakhstan. The country is notoriously corrupt. It is obvious that much of it mineral wealth has been diverted for the benefit of the President and his associates. There is a pending case against an alleged bag man who handled payoffs for US companies. However, the defendant, James Giffen, who entered a plea of not guilty in June 2004, has yet to come to trial. One has to wonder whether the size of the country's oil reserves is the real issue behind the delay.

As part of my work with the United Nations I became involved in the Abacha asset recovery case. What I discovered was that the criminal cooperation agreements were not terribly helpful to the recovery effort. The UK government stalled in providing information in what I believe was an effort to protect its financial institutions. In accordance with an agreement regarding the freezing of stolen assets, the government of Liechtenstein froze the Abacha money, but then refused to repatriate it because there have been no conviction on the "predicate" offense. The problem was that Abacha was the criminal. He died, and under common law the crime dies with the defendant. The international agreements regarding asset seizure require that there be a foreign prosecution underway and that the government asking for the seizure show that the funds are in fact tired to the crime.

Finally there is the issue of time. Each government wants to complete its investigation of the crimes associated with a bribe payment before it turns evidence over to other governments. Take the current

KBR/Nigerian bribe case as an example. The key defendant pled guilty in September of 2008. In the plea, reference is made to payments to three high Nigerian government officials between 1995 and 2002. Because of a parallel investigation in France in 2004, relating to a French partner of KBR, we know that the payments involved a company run by KBR, that was set up on the Portuguese Island of Madeira. The reports indicate that in addition a Gibraltar Company and a British lawyer are involved. The Nigerian officials said to have received the money remain unidentified.

The Nigerian request is now on temporary hold because of the "ongoing" investigation. Assuming that the Department of Justice delivers the information to Nigeria in short order the Nigerian investigation will then cut across France, the UK , Gibraltar, and Portugal. And that just covers what we now know. Most likely the money trail will move through a few more secrecy havens. With luck the criminal case in Nigeria may take form sometime in 2011 or 2012, assuming all the governments involved deliver, and the trail of the money does not involve too many more jurisdictions.

Will there be any money left to recover by the time the case is concluded? How effective will the punishment be if the case in concluded 15 years after the event?

The issue is a pressing one for Nigeria because it has cast a cloud over at least three governments. Quite properly, the US has not named the alleged recipients of the bribes. Imagine the problems that naming the alleged recipients would create if it was later learned the money in fact siphoned off by as yet unidentified middlemen.

And although many Americans will question the effectiveness of the Nigerian criminal justice process, the Nigerians on the receiving end of the charges deserve the right to defend themselves and their reputations. Nigerian citizens deserve knowing how their national patrimony came to be misused.

The Patriot Act

The financial provisions of the Patriot Act were a huge step forward in controlling the flow of funds derived from criminal sources. Every financial institution now monitors its customers' transactions and reports suspicious transactions to FINCEN. Based on my own experience, most institutions are diligent in their compliance efforts. The ones that have not been as diligent have been the target of tough enforcement actions that sent a message across the banking industry.

The transaction screening requires enhanced due diligence regarding the accounts of politically exposed persons -- so called PEPs. Suspicious Activity Reparts that result from this screening go to FINCEN for law enforcement review. From personal experience I can tell you that the US law enforcement agencies are not eager to take on the case of a foreign official living outside the United States who has suspicious bank transactions.

If an institution files a suspicious activity report they have complied with the law. The decision of what to do about the account and the customer is up to the institution. The smarter financial institutions will avoid reputational risk by closing the account and forcing the customer to go elsewhere. The money will

move and that will be the end of the story. There is nothing in the law that requires the institution to close the account.

The solution would be to hold an institution responsible for taking on a questionable account, or worse yet assisting in arranging an offshore structure for a PEP. I believe that any institution that takes on an account knowing of the likely tainted source of funds should be held responsible as the "constructive trustee" for the true owner of the money. Thus if a bank handled bribe money, the bank could be liable to repay any amount that has been moved through its facilities. The English courts have adopted this position and it does not seem to have inhibited the ability of the UK's financial institutions to operate. I also believe that after the first large recovery against a financial institution the level of care the banks will exercise will increase substantially.

Finally the Committee should be aware that most US courts dismiss cases involving foreign corruption on grounds that the case would be best tried in another jurisdiction. Congress could grant the US courts wider jurisdiction in civil recovery cases against financial institutions to make it easier on civil plaintiffs.

The most promising anti-corruption effort now under way is taking shape under the leadership of Lord Daniel Brennan, Q.C. Working with a group of non-profits he has formed a steering committee of which I am a member to create a non-profit institution to receive the assignment of the right to sue for recovery from a victimized country. It would then provide the requisite expertise, fund the recovery effort and repatriate the funds. The proposal should be ready for wider public discussion in the next several months.

global witness

Written testimony by Anthea Lawson of Global Witness for the hearing by the U.S. House of Representatives Committee on Financial Services, on 'Capital Loss, Corruption, and the Role of Western Financial Institutions'

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Mr Chairman,

My name is Anthea Lawson. I work for Global Witness, a non-governmental organisation with offices in London and Washington DC that investigates the links between natural resources, corruption and conflict. I lead our investigations on how banks facilitate corruption.

For a decade and a half, our investigations into conflict diamonds, illegal logging and corruption in oil, gas and mining have been the catalyst for international initiatives and policies to promote transparency and ensure that natural resources do not fuel conflict. Our work has been a key driving factor behind the Kimberley Process, to control the trade in conflict diamonds, and the Extractive Industries Transparency Initiative, to encourage disclosure of payments made by extractive companies and received by governments.

But with all of these investigations into various natural resource trades, there was a missing link: the route for the money behind these corrupt or conflict-fuelling transactions. So we started to look into it. And in each of these cases of corruption, there was inevitably a bank involved.

Banks are not permitted to accept corrupt funds under existing international standards, but too often they do not take this obligation seriously.

By accepting these customers, banks are fuelling corruption and therefore poverty. Countries such as Equatorial Guinea, Republic of Congo, Angola, Turkmenistan and Liberia are stark demonstrations of how banks are facilitating the looting of state assets. They are rich in natural resources, but these resources have been captured by a small minority for their own benefit, robbing these countries of crucial resources needed for development and poverty alleviation. Ultimately this creates autocracy, conflict, instability and sometimes state failure, that may require international intervention in order to protect regional security, such as occurred in Liberia. Misappropriation of natural resource revenues also affects U.S. energy and national security interests.

Six of the U.S. top ten oil importing countries rank at the bottom third of the world's most corrupt countries, according to Transparency International. An increasing amount of U.S. oil imports –now 23% of the total – come from Africa, according to Energy Information Administration statistics.

The world's poorest countries would be far less poor if revenue from natural resources that should be spent on development had not been looted by their senior government officials. In 2007, the value of exports of oil and minerals from Africa was roughly $260 billion, nearly eight times the value of exported farm products ($34 billion) and nearly six times the value of international aid ($43 billion).

Without efforts to ensure that countries can harness their own natural resource revenues rather than seeing them lost to corruption, U.S. taxpayers' money provided in aid is effectively subsidising and legitimising corruption, propping up basic state functions while leaving the rulers get on with the more lucrative business of stripping the state of its assets. Global Witness's research in Cambodia demonstrates this effect in action. Our recent report *Country for Sale: How Cambodia's elite has captured the country's extractive industries* shows how Cambodia's donors, which include the U.S., have repeatedly failed to make their aid dependent on measurable improvements in governance. Meanwhile, NGOs, including Global Witness, have continued to document that Cambodia is being run by a kleptocratic elite that generates much of its wealth via the seizure and sale of public assets, whose proceeds are then illicitly diverted into the pockets of senior officials.

I will present three examples from the latest Global Witness report, *Undue Diligence: How banks do business with corrupt regimes*. They show that heads of state and their family members from some of the world's most disturbingly corrupt regimes have been able to do business with some of the world's major banks. By doing business with these customers, these banks are facilitating corruption and therefore poverty in some of the worst-governed countries in the world.

Why is this happening? Because, quite simply, these banks are accepting these customers. There is a raft of anti-money laws in place, but somehow, banks are still able to do business with these customers. The regulations require banks to do due diligence to identify their customer and his or her source of funds, and to file a suspicious activity report if they suspect the funds are tainted. The questions we are asking, and which we would urge this committee to consider, are:

- Is fulfilment by banks of these regulatory requirements, as they currently stand, enough, in reality, to prevent banks doing business with corrupt customers?
- Is enough being done by regulators to ensure that banks do not do business with corrupt customers?

Another issue that our report explores is the way that even though the U.S. has taken steps to tighten its anti-money laundering framework, this may be undermined if other jurisdictions, including those in Europe with whom the U.S. works most closely, do not take them too. This applies not just to having appropriate regulations in place, but also to making sure that they are implemented and enforced. One of the banks that I will talk about in the following examples is a U.S. bank. But others are European, and have taken, or kept, business that has been demonstrated by U.S. enforcement

actions to be highly risky. The U.S. must therefore use its influence in the international community to make tackling the proceeds of corruption a global priority.

Overall, our research has shown that the key factors that are allowing banks to do business with corrupt regimes, and thus to help perpetuate poverty, are also precisely those which have allowed banks to destabilize the U.S. and other major economies. These are, on the part of the banks, a failure of the culture of due diligence, and on the part of the regulators, a failure of inconsistent national-level regulations to get to grips with global flows of money.

It is now universally acknowledged that there must be action to reassess the way that we regulate banks, both at the national level, and at the level of international cooperation. There is also, however, a huge 'development dividend' to be gained by tackling banks' facilitation of corruption at the same time. Mr Chairman, we welcome the fact that by holding this hearing on the proceeds of corruption at this time, this committee effectively recognizes this. While dealing, as it must, with the problems that banks have created for the U.S. economy, the U.S. government now has an opportunity to help lift millions of people out of poverty in the developing world, in a way that aid flows will never achieve.

In our first example, we show that the international financial regulatory regime governing banks has not put into place effective procedures to prevent them from handling the proceeds of corruption as have been used to stop the handling of terrorist funds. Of course the threat of terrorist finance requires ongoing attention, but corruption, at the levels we are talking about, has a devastating effect on the economic wellbeing of these countries. This has knock-on effects on the stability of these countries, on several of which the U.S. is dependent for its energy security.

Denis Christel Sassou Nguesso is the son of the President of Republic of Congo, a west African state that earns at least $3 billion a year from its oil but where a third of the population do not live past the age of forty. He is responsible for marketing the state's oil.

Between 2004 and 2006, Mr Sassou Nguesso spent hundreds of thousands of dollars in luxury clothes and shoe shops in Paris, Monaco, Hong Kong and Marbella, including tens of thousands of dollars at a time in Louis Vuitton, and repeated trips to luxury Parisian bootmakers where the shoes cost about 765 euros, or a thousand dollars, a pair.

Corresponding documents show that Mr Sassou Nguesso's credit card bills were paid off out of a bank account in Hong Kong that received the proceeds of Congo's oil revenues. These revenues should have been used to lift the people of Congo out of poverty. Instead, they were spent on shoes, clothes and other luxuries. His credit card bill for just one month, July 2005, came to $32,000. This would have paid for 80,000 Congolese babies to be vaccinated against measles, a major cause of child death in Congo.

How did he do it? The documents show that he set up a shell company in Anguilla, a Caribbean tax haven, using a trust and company services provider there that was willing to hold the shares in trust for him, which disguised his identity of the company. He then opened a bank account in the company's name at Bank of East Asia, Hong Kong's third largest

bank. Money deriving from Congo's oil sales was paid into this account. We have asked the bank if it identified the ultimate beneficial owner of this account as the son of the president of Congo, but it said it could not tell us. However, bank documents show that the bank knew that the money being paid into the account came from trading in Congolese oil.

When the credit card bills came in each month, the trust and company services provider, to whom they were addressed, wrote on the shell company letterhead to the bank, instructing payment of the bills from the account. These letters are fascinating. Firstly, they name Denis Christel Sassou Nguesso – so even if the bank had failed in its duty to identify the beneficial owner of the account, which we do not know, it did definitely know whose credit card bill it was being asked to pay. Secondly, and most importantly for the purpose of this hearing, these letters were stamped, presumably by the bank, 'record of terrorists checked'.

The U.S.-led campaign to create international controls against the financing of terrorism has had results: banks are now checking their customers are not terrorists. But there has been no similar campaign to ensure that banks worldwide do not accept the proceeds of corruption. If the U.S. was to lead such a focus on the proceeds of corruption, the effects could be very powerful. There is no stamp on this document that says 'records of politically exposed persons checked.' A politically exposed person – or PEP – is a politician, senior official or their family member or close associate. PEPs are recognised in the anti-money laundering regulations as higher risk because they could, potentially, have their hand in the till. Banks are required to identify whether their customers are PEPs and, if so, to conduct enhanced due diligence on them.

Based on our investigations, Global Witness has concluded that one of the reasons this bank did not do this is because it is not subject to meaningful regulatory standards that require it to conduct sufficient due diligence to avoid its processing the proceeds of corruption. The existing standards are not meaningful, because in practice, a bank faces little threat of sanctions should it take the proceeds of corruption – a very different outcome than if it took terrorist funds. So Bank of East Asia ran Mr Sassou Nguesso's name through the terrorist lists to check that he was not a terrorist, but did not, apparently, even check Google, let alone one of the specific PEP databases, to see if its customer was a family member of the head of state as well as being a senior official of a corrupt oil-producing country. Instead, the bank went on to arrange for payment, out of an account of a company that it knew to trade in Congolese oil products, of the personal credit card bills of the president's son.

In our second example, the U.S. took action against a bank for doing business with a corrupt regime, and then a bank in Europe continued to do business with this regime and handle its funds. In 2004-5 Riggs Bank was hit with civil and criminal penalties and forced to sell itself to another bank after a devastating inquiry by the Senate Permanent Subcommittee on Investigations exposed how Riggs held accounts for President Obiang of Equatorial Guinea and his corrupt government, and the Equatorial Guinea accounts were ordered closed. This inquiry uncovered numerous multi-million dollar suspicious transactions made out of Equatorial Guinea's oil accounts, which were under the personal control of the president, including payments to his family members. It made it clear that the Obiang family treated the country's oil revenues as if they were their own personal property. Over the last decade, Equatorial Guinea has become

Africa's third largest oil producer, with annual oil revenues of around $3.7 billion. Yet, life expectancy was only 50 in 2005 and the IMF reported in 2008 that there has been slow progress in meeting the Millennium Development Goals.

More than three years later, the British bank Barclays was still holding an account for Teodorin Obiang, the president's son, at one of its branches in Paris. So a U.S. bank failed as a result of holding accounts for the Obiang family, (and it has become a basic case study in anti-money laundering procedures) and a European bank continued to bank for one of its most controversial members.

Teodorin Obiang reportedly earns a salary of $4,000 a month as a minister in his father's government, yet has been able to purchase a $35 million mansion in Malibu, California, and a fleet of fast cars, including a Ferrari which he paid for partly with a cheque from his Barclays account in Paris, and three Bugatti Veyrons, one of the fastest cars in the world, for which he paid 1.2 million euros (1.6 million dollars) each. Just one of Teodorin's Bugatti Veyrons would have paid for an insecticide treated mosquito net for every child in Equatorial Guinea.

The remainder of the payment for Teodorin's Ferrari mentioned above came from an account he held in France at BNP Paribas, and another Ferrari was paid for with a cheque from his account in France at CCF Banque Privée Internationale, which has been owned since 2000 by HSBC.

Teodorin has also admitted on the record to a South African court that it is normal in Equatorial Guinea for a government minister to keep part of each government contract in his own pocket.

Global Witness has asked Barclays what due diligence it could possibly have done to reassure itself that the source of funds in this account is not corrupt, but Barclays said that it cannot tell us. We have posed the same questions to BNP Paribas and HSBC, and they cannot tell us either. To this day, Mr. Obiang still has ready access to funds, and property in the United States, as well as elsewhere. He clearly still has no problem getting banks to take deposits and transactions from him, despite all of the evidence on the record that he and his family live off funds diverted from the government.

This case illustrates the need for the U.S. to take further action internationally to ensure that all the major banking centres are operating at the same level. Without further steps, not only will the fight against corruption be ineffective, but U.S. banks will not be operating on a level playing field.

When the U.S. enacted the Foreign Corrupt Practices Act, in order to ensure that U.S. companies did not find themselves at a competitive disadvantage, the U.S. pushed for an equivalent international standard. The result was the OECD Anti-Bribery Convention. In the case of the anti-money laundering laws, there is an additional incentive to making sure that the standards are enforced at a similar level elsewhere. Doing so will not just ensure that U.S. banks do not suffer competitive disadvantage, but will also help to ensure that the U.S.'s efforts to tackle the corrupt money flows that cause such damage to developing countries are not undermined. And in the case of the anti-money laundering laws, the appropriate vehicle for ensuring international implementation and enforcement is already in existence, in the form of the Financial Action

Task Force (FATF), the inter-governmental body that sets the standards for anti-money laundering laws and performs mutual evaluations of its members' legal frameworks to ensure they meet this standard. The problem is that FATF's powers are not being effectively used.

At the end of this testimony I will make some suggestions for actions that FATF could take to ensure greater cooperation between nations to tackle the proceeds of corruption.

Our final example reviews Citibank's facilitation of banking activities that allowed Charles Taylor, the ex-Liberian president now on trial for war crimes, corruptly to divert timber revenues to his personal use during the conflict in Sierra Leone and Liberia. Liberian timber revenues were fuelling the conflict there, which was documented from 2000 onwards by Global Witness and a UN Panel of Experts mandated by the Security Council.

Taylor was arranging for his Ministry of Finance to instruct the Oriental Timber Company (OTC), one of Liberia's main timber exporters, to make its payments in lieu of tax directly into a number of other non-government bank accounts, including a two million dollar payment into Taylor's own private account at a bank in Monrovia, the Liberian Bank for Development and Investment (LBDI).

This dollar payment could not take place without LBDI's correspondent bank – Citibank in New York – through which the payment were routed, which gave Taylor the means to receive corrupt timber revenues into his own account.

In addition, payments received by OTC from its timber-purchasing clients around the world were paid into OTC's account at Ecobank, another bank in Liberia that had a correspondent relationship with Citibank in New York. It was on the public record at the time that OTC was one of the key timber companies whose activities and timber sales were fueling the fighting. Therefore, via this correspondent relationship, Citibank was also helping to facilitate Liberia's timber-fuelled conflict.

Global Witness asked Citibank what due diligence it had done on its correspondent clients LBDI and Ecobank, to reassure itself that they were able to do proper due diligence themselves on their clients. Citibank said that it was not able to tell us. But when we wrote to Ecobank to ask about these payments, it replied that it did not have any records of the payments as this had been a difficult time in Monrovia, and the office was looted a number of times and filing cabinets stolen. If filing cabinets were being stolen, it seems unclear how Citibank – or any other Western financial institution – could have reassured itself that its correspondent client was doing its due diligence properly.

When doing correspondent business, the only way that a U.S. bank can ensure that the proceeds of corruption or conflict do not enter the U.S. banking system is to do due diligence on its correspondent bank's own customer monitoring systems. This could not possibly have been done here by Citibank, yet the transactions took place regardless. So Citibank handled the proceeds of the timber sales that were fueling the civil war in Liberia and the deaths of many innocent persons

in the process. No correspondent relationship should be permitted with banks in other countries that do not have in place regulatory standards and controls equivalent to the U.S. and meeting international standards.

Tackling the problem

Global Witness has identified three key actions as necessary to curtail banks' handling corrupt funds:

- Banks must change their due diligence practices, and not treat customer due diligence solely as a box-ticking exercise. They must adopt policies so that if they cannot identify an ultimate beneficial owner of the funds, and do not have strong evidence that the source of funds is not corrupt, they must not accept the customer or the transaction.
- Bank regulations must explicitly force them to do this due diligence properly. Anti-money laundering laws must provide not just standards, but sufficiently specific procedures to ensure that banks identify the natural person behind the funds, and have strong evidence that the source of funds is not corrupt, or they must not accept the customer or transaction. Such standards need to be in place internationally, and applied consistently across all relevant jurisdictions, as a condition of access to the international payments system.
- International cooperation must improve, to close the loopholes in the global anti-money laundering net that are created by jurisdictions with insufficient laws or enforcement of them, and by banking secrecy and tax havens.

Global Witness wrote last year to the world's top 50 banks (as measured in July 2008) to ask them if they had a policy of prohibiting accounts for heads of state or senior officials or their families from countries with a reputation for large-scale corruption. Of the sixteen that responded, (only one of which was a U.S. bank – JP Morgan Chase), all but one did not explicitly answer the question. Rabobank, a Dutch bank, admitted that it did not have such a policy in place.

Banks are not going to tackle this issue on their own. Therefore the responsibility lies with governments to ensure that there is an appropriate standard that explicitly requires banks to avoid the proceeds of corruption, and with their banking regulators to ensure that banks are implementing this standard.

What the U.S. needs to do

There are two arenas in which the U.S. can take action to help curtail the flows of corrupt funds that are so devastating to some of the poorest countries in the world and which leave the financial system open to other types of destabilising risk.

Domestic action:

The U.S. has relatively strong anti-money laundering laws in place, in the form of the Bank Secrecy Act as updated by the Patriot Act and the subsequent rulemaking. It has also taken the lead, compared to other countries, on enforcement actions. However, at its last FATF evaluation in June 2006, the U.S. was still found to be only partially compliant with FATF Recommendation 5, which requires countries to require their banks to do customer due diligence. The U.S. should clarify its AML regulations, particularly relating to Section 312 of the Patriot Act, to make it absolutely explicit that banks must not only identify an ultimate beneficial owner, but **also** have strong evidence that the source of funds is not corrupt,

before accepting any deposit. The U.S. must also ensure that its banking regulators do effective monitoring and enforcement to ensure that banks are complying with these requirements.

International action:

The U.S. is the largest single contributor and driving force behind the Financial Action Task Force (FATF), the intergovernmental body that sets the international standard for anti-money laundering laws and measures member states' compliance with them. It should use this influence to ensure that FATF undertakes further steps to make anti-corruption rules on money laundering more stringent, including by:

- Setting up a task force specifically to address the proceeds of corruption.
- More effectively using its power to name and shame member countries that are not compliant with FATF's standards or that are not enforcing them. The majority of FATF's members, including the U.S., are not fully compliant with key FATF recommendations relating to the prevention of corrupt flows, including Recommendations 5 (customer due diligence), 6 (identification of and enhanced due diligence on Politically Exposed Persons) and 33/34 (prevention of misuse of corporate vehicles and legal arrangements such as trusts).
- Ensuring that FATF evaluations measure implementation and enforcement of anti-money laundering laws and not just their presence on a country's statute books.

The U.S. should also use its position within FATF to push for **new standards** within the international framework:

- Banks should be required to respond to requests for information from foreign banks or their own overseas branches without falling foul of banking secrecy laws, whether the request is about money laundering, terrorist financing or tax fraud (this would effectively internationalize provision 314 of the U.S. Patriot Act).
- The FATF should adopt the recommendation that every country produce full public online registers of the ultimate beneficial ownership and control of all companies and trusts under its jurisdiction. Currently, in the U.S. there is no such requirement, and the ultimate beneficial ownership of these vehicles is very often not subject to any form of public disclosure. One result is that U.S. trusts and limited liability companies are frequently abused by criminals, drug traffickers, corrupt officials, and tax cheats to launder money through banks in other jurisdictions, including many of those most criticized by the U.S. as bank secrecy havens. The U.S. currently is not compliant with the existing relevant FATF standard (Recommendation 33/34), and has taken minimal steps to achieve compliance in this area, facilitating billions of dollars of money laundering a year through trusts and companies established in the U.S. The proposed S.569 Incorporation Transparency and Law Enforcement Assistance Act Bill would go some way towards remedying this, but it would not have such registries held publicly, which would be the most effective standard.
- Banks should be required to be aware of which countries have laws prohibiting their PEPs from holding bank accounts abroad, and to avoid accepting these PEPs as clients.

Current efforts to modernize regulatory practices in the financial sector offer the U.S. and the international community a significant opportunity to address the problems that are allowing the financial system to be a conduit for corrupt funds. If

this opportunity is not taken, the global financial system will be left open not just to the proceeds of corruption but to the opaque financial flows that have contributed to the immediate crisis, as well as to terrorist and proliferation finance.

Global Witness would also like to point out that taking action to combat corrupt money flows must go in parallel with efforts to ensure transparency of oil, gas and mining revenues. Promoting greater accountability of how oil, gas and mining revenues are managed is also crucial to promoting poverty alleviation in poor, resource-rich countries and helping ensure U.S. energy security. Mr Chairman, we commend you for the leadership you have shown on this issue through the introduction of H.R. 6066 – the Extractive Industries Transparency Disclosure Act - in the 110th Congress. This legislation would require oil, gas and mining companies registered with the Securities and Exchange Commission to publicly disclose their payments to countries where they operate, on a country-by-country basis. We hope that H.R. 6066 will be re-introduced this year and urge Congress to pass this important piece of legislation.

We would be pleased to see this committee take up these issues, and I would be pleased to answer any questions.

Detailed references for the case studies mentioned in this testimony are available in Global Witness, *Undue Diligence: How banks do business with corrupt regimes*, March 2009 (London)

global witness

Annex to the written testimony by Anthea Lawson of Global Witness for the hearing by the U.S. House of Representatives Committee on Financial Services, on 'Capital Loss, Corruption, and the Role of Western Financial Institutions'

May 19, 2009

- An example of Denis Christel Sassou Nguesso's credit card statements: month of August 2006.
- Company information sheet for Denis Christel Sassou Nguesso's Anguillan shell company, Long Beach.
- Trust document showing Denis Christel Sassou Nguesso's beneficial ownership of the shell company, Long Beach.
- Bank of East Asia 'Data Archive and Retrieval System: Daily Transaction Journal' showing payment referencing a specific oil cargo into the Long Beach account.
- Payment instruction from Long Beach to Bank of East Asia instructing payment of Denis Christel Sassou Nguesso's credit card bills from the Long Beach account, stamped 'record of terrorists checked'.
- French police document listing Teodorin Obiang's bank account at Barclays.
- Letter from the Liberian Ministry of Finance to the Oriental Timber Company instructing payment of $2 million in lieu of taxes into an account at Liberia Bank for Development and Investment, routed through Citibank.
- Debit ticket and bank statement showing the $2 million payment from the Oriental Timber Company into the account at Liberian Bank for Development and Investment, which is named as Charles Taylor's personal account.

Online Credit Card Limited
聯網信用卡有限公司

「繳費靈」商戶編號 PPS Merchant Code : 78
http: //www.olcreditcard.com

RECEIVED
07 SEP 2006

CREDIT CARD NUMBER	STATEMENT DATE	PAYMENT DUE DATE
5430 9600 6810 1330	02/09/2006	IMMEDIATE
	STATEMENT BALANCE	**MINIMUM PAYMENT**
	$35313.36	$35313.36
	AMOUNT ENCLOSED	**CHEQUE NUMBER**

DENIS CHRISTEL SASSOU NGUESSO
ICS TRUST (ASIA) LTD
8/F HENLEY BLDG
5 QUEEN'S RD
CENTRAL HONG KONG

☐ Tick the box for change of address or other requests. See reverse side.
若需要更改地址或其他事項，請於格內加「✓」。詳情請參閱背頁。

Crossed cheque should be made payable to "ONLINE CREDIT CARD LIMITED" and returned with this payment slip to P.O. Box 54379 North Point Post Office, Hong Kong at least three working days before "Payment Due Date". All cheque payments are subject to collection.
劃線支票請開出抬頭付款單據予「聯網信用卡有限公司」，三個工作天期間交香港北角郵政局郵政信箱54379 收妥。劃線支票請開出抬頭「聯網信用卡有限公司」。支票付款，收妥作實。

7

CREDIT CARD NUMBER	CREDIT LIMIT	STATEMENT DATE	PAYMENT DUE DATE	MINIMUM PAYMENT	
5430 9600 6810 1330	$50000	02/09/2006	IMMEDIATE	$35313.36	1

USD GOLD

	OPENING BALANCE				4021.44
03/08/2006	LOUIS VUITTON ESPANA	RIO VERDE	EUR	10000.00	13081.52
09/08/2006	PAYMENT - THANK YOU				4020.14-
10/08/2006	R.CAVALLI-PRINCESSE BO	MARBELLA	EUR	7264.00	9438.63
27/08/2006	LOUIS VUITTON ESPANA	RIO VERDE	EUR	1870.00	2430.98
27/08/2006	LOUIS VUITTON ESPANA	RIO VERDE	EUR	3310.00	4302.97
28/08/2006	BRIONI ESPANA	MARBELLA	EUR	4660.00	6057.96
	TOTAL CHGS : DENIS CHRISTEL SASSOU NGUESSO			35312.06	
	CLOSING BALANCE				35313.36

ALL AMOUNTS ARE INDICATED IN US DOLLARS, UNLESS OTHERWISE STATED.

Please examine this statement immediately. If no error is reported within fourteen days, this statement will be considered to be correct. If you have any questions, please call the Online Credit Card Customer Service Hotline at 2563 3633.
請收到月結單後，請即查閱單據是否正確無誤。若本公司於發出月結單後14日仍未收到閣下之通知，一切賬項均作實論。如下如有任何查詢，請即致電聯網信用卡客戶服務熱線 2563 3633。

COMPANY INFORMATION SHEET

CIS-1
As of 11/12/2006 (17:14:09) Page 1

Company: LONG BEACH LIMITED

Address: 8th Floor Henley Building 5 Queen's Road Central, Hong Kong

Jurisdiction of Incorporation:	Anguilla	***Incorporation Date:***	03/03/2003
BRC #:	- -	***Certificate #:***	2029959
Employer's File #:			
ProfitsTax File #:			

Authorized Share Capital

USD 1,000,000.00	=	1,000,000	Ordinary shares at	USD 1.00

Issued Share Capital

USD 2.00	=	2	Ordinary shares at	USD 1.00

Secretaries

ICS Secretaries Limited

Shareholders

Orient Investments Limited	1	Ordinary share
Pacific Investments Limited	1	Ordinary share

Directors

Orient Investments Limited

Pacific Investments Limited

Banking Information

Account No.	***Banker / Branch***	***Account Type / Currency***	***Date Opened***
015-514-25-10518-6	The Bank of East Asia, Limited / Main	Statement Savings Account / MYC	17/11/2003

Signatory: Orient Investments Limited to sign singly

ICS

DECLARATION OF TRUST

WE, **ORIENT INVESTMENTS LIMITED**, of The Hallmark Building, Suite 227 Old Airport Road, The Valley Anguilla, British West Indies DO HEREBY SOLEMNLY AND SINCERELY DECLARE as follows:

1. THAT the 1 share(s) denominated as **No. 001**
   now held by us
   in: **LONG BEACH LIMITED**
   does not belong to us, but
   to: **Denis Christel Sasson-Nguesso**
   of: 20 Bis Rue Jean Giraudoux 75016 Paris France.

   who is hereinafter referred to as the BENEFICIAL OWNER which expression shall include his personal representatives, successors in title and assigns.

2. THAT we hold the said share(s) UPON TRUST for the said BENEFICIAL OWNER AND we undertake to transfer pay and deal with the said share(s), dividends and interest in such manner as the BENEFICIAL OWNER shall from time to time direct AND WE FURTHER UNDERTAKE THAT we will at the request of the BENEFICIAL OWNER attend all meetings of shareholders which we are entitled to attend by virtue of being the registered holder of the said share(s) and will vote at in such manner as directed by the BENEFICIAL OWNER.

   In witness whereof we have caused our Common Seal to be hereunto affixed on this 24 September 2003.

Sealed with the Common Seal of
Orient Investments Limited
signed by
Eliza S. Y. Wu
for and on behalf of the company
in the presence of:

) For and on behalf of
) **Orient Investments Limited**
)
)
)
)

Witness: Mila G. Rehman
Address: 8th Floor Henley Building 5 Queen's Road Central Hong Kong

Page: 1 Document Name: untitled

DATA ARCHIVE AND RETRIEVAL SYSTEM
BANK OF EAST ASIA
DAILY TRANSACTION JOURNAL

OUR REFERENCE NO. & SUB-NO.	TT50412669-00
REMITTING BANK CODE	PNB1
THEIR REFERENCE	050408187432000A
CURRENCY CODE	USD
AMOUNT	149,944.19
VALUE DATE	050412
REIMBURSING BANK CODE	PNB1

FXR02JL-01 /010140900 /

FX (INWARD REMITTANCE) ONLINE TRANSACTION JOURNAL
FXR02JL-01 FOREIGN EXCHANGE DEP

TRAN TIME USER ID TERMINAL ID	TRANSACTION DESCRIPTION
DATA DESCRIPTION	NEW INFORMATION
N/V A/C NO IND	N1
ORDERING CUSTOMER 1	ANTOINE JADAKAT
ORDERING CUSTOMER 2	
ORDERING CUSTOMER 3	
ORDERING CUSTOMER 4	
BENEFICIARY BANKER CODE	
BENEFICIARY BANKER NAME	
BENEFICIARY BANKER ADDRESS 1	
BENEFICIARY BANKER ADDRESS 2	
BENEFICIARY BANKER ADDRESS 3	
BENEFICIARY NAME 1	LONG BEACH LIMITED
BENEFICIARY NAME 2	
BENEFICIARY ADDRESS	
BENEFICIARY TELEPHONE NO.	
BENEFICIARY A/C NO.	51425105186USD
BENEFICIARY SUB A/C NO.	00
ACCOUNT RATE CODE	
PAYMENT DETAILS 1	MT GENMAR SPARTIATE B/L 17.1.05 RF
PAYMENT DETAILS 2	B7TT 3054/05
PAYMENT DETAILS 3	
PAYMENT DETAILS 4	
SETTLEMENT METHOD	02
ENQUIRY MESSAGE TYPE	00
OUR AGENT INDICATOR	00
THEIR AGENT INDICATOR	00
SWIFT MESSAGE TYPE	103
INSTRUCTED AMOUNT	0.00
EX. RATE FOR INSTRUCTED AMT	0.00000000
DETAILS OF CHARGES	SHA
SENDER CHARGES 1	0.00
SENDER CHARGES 2	0.00
SENDER CHARGES 3	0.00
SENDER CHARGES 4	0.00
RECEIVER CHARGES	0.00

DEBIT VOUCHER

LONG BEACH LIMITED
Unit 1, Hartley Bldg., 5 Queen's Rd., Central, Hong Kong
Tel No. (852) 2854-4848 Fax No. (852) 2543-4080

11 September 2006

Record of terrorists checked

The Manager
The Bank of East Asia, Limited
10 Des Voeux Road Central,
Hong Kong

Dear Sir/Madam,

RE: LONG BEACH LIMITED
ACCOUNT NO.: : 015-514-25-10518-6

Upon receipt of this letter, please immediately transfer from the above captioned account to the following:-

AMOUNT	:	USD 35,313.36***(United States Dollars Thirty Five Thousand Three Hundred Thirteen and Cents Thirty Six Only.)***
BENEFICIARY BANK	:	Standard Chartered Bank (HK) Limited Hong Kong
BENEFICIARY NAME	:	Online Credit Card Limited
ACCOUNT NO	:	317- 1- 008809- 7
MESSAGE	:	Payment of Online CC: Denis Christel Sassou Nguesso A/C # 5430 9600 6810 1330

Please deduct all bank charges from the above-captioned account.

Should you have any quaries on this matter, please contact **the Client Treasury Department at 2854 4544.**

Please deduct all bank charges from the above-captioned account.

Thank you for your co-operation.

For and on behalf of
LONG BEACH LIMITED
By: Orient Investments Limited

(Authorised Signatory/ies)

E.T.B.B. FOR BANK USE ONLY	
Reference No. BEMO14-	07/190-00
Value Date	11 SEP 2006
Exchange Rate	
HKD Equivalent	
Service Charges	70
Commission (Swiftfee)	1.67
Postage / Cable	130
Additional Handling Charges	200
Total HKD	
Paying Bank	STANDARD CHARTERED BANK (HK) LTD H.K.
Covering Bank / Demand Draft Drawn On	CITIBANK NA NEW YORK
Received by for and on behalf of The Bank of East Asia, Limited	11 SEP 2006
Authorised Signature	

REPUBLIQUE FRANCAISE

MINISTERE DE L'INTERIEUR

DIRECTION GENERALE DE LA POLICE NATIONALE

N°132/2007/D/7

AFFAIRE :

Recel de détournement de fonds publics

OBJET :

:EPONSE A REQUISITION CONCERNANT :S COMPTES BANCAIRES DE **TEODORE OBIANG** ET **TEODORE NGUEMA OBIANG**

PROCES VERBAL

L'AN DEUX MILLE SEPT, le trois octobre,

à ////////////////////// heures,

NOUS : **Stéphane VACHON**
Capitaine de Police
En fonction à la Direction Centrale de la Police Judiciaire

Office **C**entral pour la **R**épression de la **G**rande **D**élinquance **F**inancière
Plate-forme d'Identification des Avoirs Criminels

Officier de Police Judiciaire en résidence à Paris,
Nous trouvant à Nanterre,

Poursuivant l'exécution du Soit Transmis N°P0708792027 délivrée le 18 juin 2007 par Monsieur J.M. ALDEBERT, Vice Procureur près le Tribunal de Grande Instance de Paris, enquêtant sur des faits de recel de détournement de fonds publics.
Vu les articles 16 à 19 et 75 à 78 du code de Procédure Pénale,
Vu l'article 77-1-1 du code de Procédure Pénale,

Pour faire suite à notre réquisition à la Direction Nationale des Enquêtes Fiscales (DNEF) accompagnée d'une liste de personnes physiques appartenant à la famille de M. Téodore OBIANG, avons reçu les informations suivantes concernant les comptes bancaires (FICOBA).
OBIANG Teodoro n'est pas titulaire de compte bancaire en France.
Son fils, **NGUEMA Teodoro** né le 24/06/1969, est titulaire du compte suivant :

30588 61024 61483680101	13/09/1989	Compte courant	Barclays Bank PLC	Ternes Saint Honoré	217 rue du Faubourg saint Honoré 75008 Paris	Malabo (Guinée Equatoriale) (au 13/09/1989)

Dont procès verbal.

Le Capitaine de Police,

POLICE NATIONALE
DIRECTION CENTRALE DE LA POLICE JUDICIAIRE

REPUBLIC OF LIBERIA
MINISTRY OF FINANCE
MONROVIA, LIBERIA

July 6, 2000

Mr. John Teng
General Manager
Oriental Timber Corporation
Grand Bassa County

Dear Mr. Teng:

RE: GOL TAX PAYMENT TRANSFER

You are hereby authorized to transfer the amount of US$2,000,000.00 against forestry related taxes to Liberia Bank for Development and Investment, a/c#0020132851-01 through:

Citibank
399 Park Avenue
New York, N. Y. 10043
USA

This amount is due in taxes to the Government of Liberia. Flag receipts will be issue your corporation as evidence of payment, as soon as acknowledgment is received from the bank.

Kind regards.

Very truly yours,

Juanita E. Neal
Deputy Minister/Revenue

THE LIBERIAN BANK FOR DEVELOPMENT & INVESTMENT
P. O. BOX 547, MONROVIA, LIBERIA

DEBIT TICKET DATE: 7/18/00

DEBIT: RAD — 211112

OFFSET (CREDIT): CHARLES G. TAYLOR 00-201-32851-01

DETAILS: BEING, RAD REF # CD001991535601 IWO COL B/O NATURA HOLDING & PTE LTD A/C CBM with 7/17/00

ONE MILLION NINE HUND- NINTY NINE THOUSAND NINE HUND SEVENTY FIVE DOLLARS

AMOUNT IN WORDS

US$1,999,975-00

AMOUNT IN FIGURES

MAKER CHECKER OFFICER

AUTHORIZED SIGNATURE

ORIGINAL

LIBERIAN BANK FOR DEVELOPMENT AND INVESTMENT

HEAD OFFICE BRANCH (US DOLLAR)
Ashmun & Randall Sts.
P. O. Box 547
Monrovia, Liberia

For Correspondence
Call us at 227119
or Fax us at
Bank Sort Code: 000-000

00.201-32851-01 (32851-01)
TAYLOR, CHARLES G.
US DOLLAR
CHECKING ACCOUNTS - PERSONAL

CHARLES G., TAYLOR
CONGO TOWN

MONROVIA,LIBERIA

THIS STATEMENT COVERS 01 Jul 2000 THROUGH 31 Jul 2000

Trx Date	TxRef	Details	Chq No	Value Date	Debits	Credits	Balance	Payee
Jul 2000								
01	0000	BALANCE B/F				2,274.32	2,274.32	
11	19377	COMM ON TOD			-2,000.00		274.32	
11	19389	T6 CHECK CASHED	033532		-100,000.00		-99,725.68	
11	19389	PER DEBIT CHARGE			-1.10		-99,726.78	
17	20671	T2 CHECK CASHED	033536		-250,000.00		-349,726.78	
17	20671	PER DEBIT CHARGE			-1.10		-349,727.88	
18	20856	RAD INO C.G.T. B/O NATURA HOL				1,999,975.00	1,650,247.12	
18	20883	COM ON RAD DD 7/17/00			-26,999.66		1,623,247.46	
18	20883	PER DEBIT CHARGE			-1.10		1,623,246.36	
18	20752	T5 CHECK CASHED	033551		-240,000.00		1,383,246.36	

The Committee on Financial Services

Hearing "Capital Loss, Corruption, and the Role of Western Financial Institutions"
May 19, 2009, 10 AM
- Monica Macovei

Measuring corruption.
Surveys on individuals', groups' and companies' experience and perception have been regularly used to measure corruption. Corruption Perception Index, Global Corruption Barometer, World Bank Doing Business Reports, Freedom House - Nations in Transition are among the best known instruments.

In addition to measuring the perception of the public or the business communities, corruption can be identified and its dimension measured by scrutinizing those areas with high potential or risk of corruption, such as: (i) privatizations and public procurement (some of the indicators could be: the avoidance of public tenders and the direct attribution of contracts, a price much higher than the market price or the highly inbalanced parties' contractual duties and rights); (ii) the transfer/sale of real estate property from the public property to the private property or the public/private property partnerships (one indicator of possible corruption/fraud in this area being a grossly sub-evaluated price or value for the public property to be transferred and/or the existence of conflict of interest); (iii) the level of transparency and the control over the public spending (a poor transparency and a superficial and late control are possible signals raising questions); (iv) the funding of political parties and electoral campaigns (where the control is not sound and the sanctions are not deterring); (v) the control of the public officials' declarations of assets and statements of interests (where such control fails to be sound and/or impartial), or; (vi) the existence of the so called „laws with destination".

Sources of corruption
The sources of corruption I have indentified are strongly linked with the areas identified as having a high risk of corruption: illegal behavior in privatizations, public procurement and where transferring the state/public property by the central or local administration or other public bodies; incomplete transparency of the public spending and lack of control and accountability; a poor legal and institutional framework for the financing of political parties and electoral campaign; the failure to institute and exercise a sound control over the declarations of assets of the public officials and civil servants and the lack of deterring sanctions where unjustified assets are proved; the existence and the failure to sanction the conflict of interest and the incompatibilities; poor, not-unified and unequal enforcement of legal provisions; instable legal and institutional framework, etc. Under this item, I would like to refer to the finding of the UNODC 2008 report (focusing on the organized crime in Balkans), on the "wide-spread and enduring collusion between politics, business and organized crime. To break this nexus, fighting corruption should be priority number one".

As regards the circumstances which, taken together, favored corruption, in particular the political corruption (corruption influencing the decision-making process and actors), in some of the post communist countries, I would refer to: the dimension of the state property to be transferred from the state to private hands during the transition to the market economy; the need of building or re-building the infrastructure, involving large amounts of funds (first two seen as "unique" opportunities; the poor and changing legal framework on public procurement; the weak and in-transition law enforcement and judiciary at the beginning of 1990s; the low level of accountability in fragile democracies.

Problems encountered in discovering, disclosing and deterring corruption in Romania
Corruption has been investigated and prosecuted by the Romanian law enforcement in particular since 2005/2006, by the Anti-Corruption National Directorate, a law enforcement unit with jurisdiction over medium and high level corruption and fraud, formed of specialized and trained prosecutors and police, who also benefited of technical support from the US State Department. Approximately 20 ministers and parliamentarians ("sitting" and "former" at the time of the prosecution) were indicted for corruption or fraud in the last three years, along with many other high officials in the central and local administration, police or members of the judiciary, as well as heads and administrators of companies. These prosecutions have been a premiere in Romania.

However, deterring sanctions did not come. Once before the courts, the high political corruption cases in particular have not received solutions on the merits. Instead, they have been postponed for months and even years, for a variety of reasons: (i) the reluctance of some judges to take decisions on the merits in such cases (although their independence is fully guaranteed, for instance they all enjoy life tenure, and can only be disciplined by a judicial council formed of their peers); (ii) the 2007 intervention of the Constitutional Court which decided, for instance, that the rules of procedural immunity apply to former ministers as well as ministers in office[1], and stated the retroactive application of this ruling; as a result, some of the court cases returned to the law enforcement for missing the decision on the immunity lifting; (iii) while in those cases where these approvals fall into the jurisdiction of the President of the country, they were issued quite rapidly, in the cases where the Parliament had to decide (for former ministers but current MPs), it took long periods of time, sometimes over a year, for a decision to be taken; in addition, many MPs claimed they had to analyze all the "evidence", acting like courts; (iv) in the corruption cases where the courts convicted the defendants, 80% of the sentences have been suspended prison sentences, indicating that corruption is not seen by the judiciary as a serious offence.

In parallel to the law enforcement investigations in high level political corruption cases, the legal stability and efficiency of the anti-corruption (and anti-crime in general) framework was endangered by a Chamber of Deputies' 2007 decision which amended, at its own initiative, the criminal procedure code, introducing, for instance, the rule that interceptions could only be possible after the person under investigation had been informed that an investigation takes place. This and other provisions constituting strong obstacles against criminal investigations (and international police and judicial cooperation in cross border organized crime) did not enter into force following the President's decision to return the law to the Parliament and request its re-examination. Among others, the then US Ambassador and the European Commission also sent public signals on the danger of adopting such provisions which would at least hamper the efficiency of international cooperation in criminal cases. Those provisions are not in force, but the attempt to take away important instruments in the fight against corruption and organized crime was clear.

At present, new drafts of the criminal and criminal procedural codes are under debate.

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[1] As found by a 2007 Peer Review Report issued by an independent expert in the context of the Cooperation and Verification Mechanism established jointly with the European Commission for the post EU accession period for Romania, "this decision does not seem very logical. The procedural immunity for ministers derives from the need to protect ministers in office against criminal investigation based upon politically motivated complaints and to avoid that political decision-making at the highest level would be influenced in this way. Once a minister is no longer in office, political decision-making can no longer be influenced in this manner, so there is no longer any need for procedural immunity."

Pressures/dangers faced "on the ground" by the anti-corruption advocates and watchdogs

While there have not been examples of people being in "danger", I could point out to the pressure exercised, through public statements or attempts to change the legal and institutional anti-corruption framework by the politicians under investigation and their party colleagues. However, I have to say that I find this predictable, as well as being a proof of the seriousness and partially successful attempt to fight corruption starting from the top.

If I look at myself as an "anti-corruption advocate" (and I do), I would say that I was fired - through a reshuffle of the Government, eliminating the party which supported me in the position of justice minister- following the anti-corruption measures I have adopted and promoted. This took place shortly after January 1st, 2007, when Romania joined the European Union due, among others, to the results (prosecutions and legislation) in the fight against high level corruption.

The Slovenian Commission for Prevention of Corruption, entrusted with control of conflicts of interests of elected politicians, was saved by the Constitutional Court, as MPs after accession promptly voted for its closing down. In Latvia, a success story for anticorruption in the EU accession years, the public had to rally to defend the anticorruption agency head from being fired by the Prime Minister. However, the second attempt, in 2008, was successful.

To what extent did the change of regime in Romania represent a true change from a corrupt regime to a regime with higher ethical standards?

If one refers to the change of regime in 1989, the changes are tremendous, even if obtained through a long transition process and even if we are still struggling for real and profound reforms in areas such as health, education or judicial systems. Among others, the independent judiciary (even if still lacking efficiency, predictability and sometimes integrity), investigative media, civil society, have all contributed in time to disseminating higher ethical standards. However, the transition favored and produced corruption, in the circumstance I explained previously. I believe that the main challenge ahead is the reform of the political class and the establishment of a solid good governance.

Does growing corruption in the political elite transfer to changes in the ethical climate in society as a whole?

The brief answer would be yes, in particular under the circumstances where the society does not see a quick process and deterring sanctions for corruption. In addition, the feeling shared by many that, for instance, quality and timely services need more than a correct request is not helping to reach a general ethical climate. Once again, I believe that the challenge we have for building a sustainable ethical climate is the reform of a large part of the political class.

Capital Loss and Corruption: The Example of Nigeria

Testimony before the House Financial Services Committee

May 19, 2009

by

NUHU RIBADU

Visiting Fellow at St. Anthony's College, University of Oxford; Visiting Fellow at the Center for Global Development; and former Executive Chairman, Economic and Financial Crimes Commission (EFCC) of Nigeria

Good morning, Chairman Frank, distinguished US Representatives of the Committee, and thank you for this very kind invitation to offer testimony as part of this panel.

The global financial crisis has made nothing so clear as the fact that the global economy is now highly integrated and interconnected. What effects one corner of the globe will reach to all other corners, and the lack of proper regulation and oversight in one place can undermine stability far away.

Corruption has the same effect on global markets, although it is not often thought of in those terms. So just as it is the purpose of this hearing to explore lines of responsibility in the global financial crisis, so too should it be to better understand the global responsibility to end corrupt practices.

Understanding corruption as a transnational problem is the only way to fight it. Corruption in one place is connected to others, enabled by systems of weak regulation and poor oversight. When you think of "corruption," there will always be specific personalities and places that jump to mind, and inevitably Nigeria is

near the top of that list. But I think you will all agree with me that corruption is not a native of any land; it just finds easier homes in some. Societies that have been able to move ahead are those that put the statutes in place to criminalize corruption and ensure that the enforcement mechanisms are proper and ready for action.

Let it be clear from the onset that my intention is not to speak ill of my country or continent, but rather to state the facts as they are.

Next year, Nigeria will be half a century old. In 1960, the year I was born, my country attained Independence from Britain. The promise of independence was boundless and the famous Nigerian energy was all too evident. We were sure we would make it. Home to about 140 million of the West African region's 220 million inhabitants, Nigeria's demography alone elects it as a regional power.

Today, after one civil war, seven military regimes, and three botched attempts at building real democracy, there is one connecting factor in the failure of all attempts to govern Nigeria: corruption.

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Mr. Chairman, your chosen theme for today's hearing is right on target. Corruption and capital drain have been the major factors in the lack growth and development in the region. The corruption endemic to our region is not just about bribery, but about mismanagement, incompetence, abuse of office, and the inability to establish justice and the rule of law. As resources are stolen, confidence not just in democratic governance but in the idea of just leadership ebbs away. As the lines of authority with the government erode, so too do

traditional authority structures. In the worst cases, eventually all that is left to hold society together is the idea that someday it may be your day to get yours. This does little to build credible, accountable institutions of governance or put the right policies in place.

The African Union has reported that corruption drains the region of some $140 billion a year, which is about 25% of the continent's official GDP. In Nigeria alone, we had a leader, General Sani Abacha, it was believed that he took for himself between $5–6 billion and invested most of it in the western world.

With this history, the EFCC undertook the investigation and auditing of the assets of serving state governors and public officials suspected of stealing public funds. We were assisted by the London Metropolitan Police, including in two cases involving governors. Mr. Joshua Dariye, Governor of Plateau state, was found by the London Metropolitan Police to operate 25 bank accounts in London alone to juggle money and evade the law. Like many of the governors, he used front agents to penetrate western real estate markets where he purchased choice and expensive properties. The London Metropolitan Police determined Dariye had acquired £10 million in benefits through criminal conduct in London, while domestically we were able to restrain proceeds of his crimes worth $34 million. The other was the case of Mr. D.S.P. Alamieyeseigha, governor of oil rich Bayelsa State. He had four properties in London valued at about £10 million, plus another property in Cape Town valued at $1.2 million. £1 million cash was found in his bedroom at his apartment in London. £2 million was restrained at the Royal Bank of Scotland in London and over $240 million in Nigeria. This is in addition to bank accounts traced to Cyprus, Denmark, USA and the Bahamas.

These are just two examples. In 80% of the grand corruption that takes place in Africa, the money is kept somewhere else, enabled by systems of poor regulation that allow abuse by those looking for ways to profit.

Between 1960 and 1999, Nigerian officials had stolen or wasted more than $440 billion. That is six times the Marshall Plan, the total sum needed to rebuild a devastated Europe in the aftermath of the Second World War. When you look across a nation and a continent riddled with poverty and weak institutions, and you think of what this money could have done – only then can you truly understand the crime of corruption, and the almost inhuman indifference that is required by those who wield it for personal gain.

For the West to finally understand why those like myself and my colleagues here today, John Githongo and Monica Macovei, are willing to risk so much, risk our lives, to fight corruption in our home nations, the West must then be willing to see corruption as not just a system of bribes and patronage, but the systematic undermining of responsible governance, of visionary leadership, of a society's ability to meet and overcome challenges. The West must understand that corruption is part of the reason that African nations cannot fight diseases properly, cannot feed their populations, cannot educate their children and use their creativity and energy to open the doorway to the future they deserve. The crime is not just theft. It is negligence. Wanton negligence, the full impact of which is likely impossible to know.

I have said this before, and while I know it is a controversial statement, I stand by the idea that corruption is responsible for as many deaths as the combined results of conflicts and HIV/AIDS on the African continent.

I always see myself as a policeman first, and as a law enforcement officer at the frontlines, I have seen corruption provide fertile ground for injustice, for violence, for the failure of government and the failure to use revenues and donor support for the benefit of the people. I see how those who are confronted with these systems – diplomats, foreign businesses, NGOs and others with the best of intentions for the continent – make the choice to work within those corrupt practices to get the job done faster, or try to work ethically and morally while knowing this choice will cost them time, profit, and impact. I see people suffer, and while they may not know why or how exactly, they understand that it is unjust, they know right from wrong, and they know that as long as these systems are allowed to thrive, their lives will never be better. But so long as bowing to corruption is the primary way of succeeding in certain societies, it trains generation after generation to accept its yolk, get their due, and ignore those around them.

On a regional dimension, it is estimated that some $20 billion leaves Africa annually through the illicit export of money extorted from development loan contracts. This money is deposited in overseas banks by a network of politicians, civil servants and businessmen. This figure is now roughly equal to the entire amount of aid from the US to Sub-Saharan Africa every year.

This outflow is not just abstract numbers: it translates to the concrete reality of kids who cannot be put in schools, who will never learn to read, because there are no classrooms; mothers who die in childbirth because the money for maternity care never made it to the hospitals; tens of thousands who die because there are no drugs or vaccines in hospitals; no roads to move produce from farms to

markets or enable a thriving economy; no jobs for young school graduates or even ordinary workers; and no security for anyone because the money has been stolen and shipped out.

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The picture I paint here is that of my country. The picture of a potentially great land, slowly poisoned by the idea that the importunity of lawlessness is success. The picture of a land held hostage for decades by a kleptocratic bunch of fraudsters who built a career in politics to protect their lines of revenue. I am saddened when I hear America's new president, his First Lady, and his cabinet officials all speaking at graduation ceremonies and calling for service to your country and your community, because I know that in Nigeria that this is not happening at the moment.

While there is much blame to be directed at Nigeria for this state, we should not stand accused for these crimes alone. The unholy alliance between local political elites and western financial institutions has been the foundation of this narrative of shame. The best illustration yet is the now famous Halliburton/KBR scandal where, as a Nigerian Newspaper recently reported, our leaders received "stacks of US dollar bills in briefcases and sometimes in bullion vans" until some $185 million had been exchanged for a contract to build a liquefied natural gas plant.

The other famous case is the Siemens scandal. According to the US Securities and Exchange Commission [SEC], Siemens made approximately $12.7 million in "suspicious payments" for Nigerian projects, including to government customers for four telecommunications projects. The total value of the four contracts was

approximately $130 million. There are many other instances. The total amount in bribes is staggering.

In both of these cases, the United States and Germany, the parent nations of these two companies, have initiated stern investigations and issued out hefty fines on the companies – but those who received the bribes in Nigeria continue to enjoy the fruits of their labors, which only means the cycle will continue. It is clear that KBR did their own calculus: $185 million in bribes, plus eventually almost $600 million in fines for violation of the Foreign Corrupt Practices Act, but they won $6 billion in business for their efforts. These projects continue on. And this kind of math will continue on for as long as companies realize there are those on the ground willing and eager for this type of facilitation. In Nigeria, the alleged culprits are going about their daily lives and even running the government by default. And yet they are still engaged from outside as equal partners in governance and development.

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I have always held the belief that the laws needed to check these problems often already exist; what is lacking is the culture of enforcement. Enforcement blossoms only where there is the necessary political will, and this political will must be strong at the very top. There is no place in the world where anti-corruption efforts will succeed without this political will, without leadership to promote the effort openly as a moral and political force. Without this will, the pressure on enforcement agents smothers their efforts and is destined to destroy the very agencies defined to lead the war against graft.

I learnt this myself by firsthand example. Having spent five years building Nigeria's EFCC into a world-class crime-fighting agency with trusted partnerships with US and UK agencies, all of it has now changed, like many of the other reform efforts in the country.

When the EFCC was formed in 2003, our country had never secured a single criminal conviction for corruption charges. We were fortunate to have the political support of President Obasanjo; of other several powerful ministers in the government including Nasir El-Rufai, from whose budget the original money to support the EFCC came; from key Senators; and from the judiciary whose responsibility it was to decide the cases presented to them.

By 2007 we had secured convictions in over 275 of the near 1000 cases in the courts. It was modest but revolutionary, especially since the convictions were from cases against high-ranking officials such as the leadership of the Nigeria Police, a number of state governors, ministers, legislators and top bureaucrats. The symbol of these convictions to ordinary Nigerians had more impact than I could have believed. But for the first time, they saw those living unlawfully and with impunity being called to task, and they allowed themselves to hope that a new Nigeria, where the fruits of their labors would finally be enough to prosper, may be coming.

And things changed, at least for a while. This was homage to the extraordinary will and belief of young Nigerians who saw corruption as the barrier to the progress of our country and wanted to contribute. The effort we made at the EFCC was a marriage of two forces: pressure from outside and the force from within. The international community deployed the instruments of the Financial

Action Task Force [FATF] to trigger necessary reforms, which provided us the platform to build a strong local program to clean up our financial institutions and prosecute those who sought to undermine them. This ultimately paved the way for a far-reaching banking reform in the country, famously described as the consolidation of about a hundred mushroom banks into 25 strong institutions. Some of these banks are now seen as credible financial institutions with continental reach; indeed, some of them are stepping in to fill the gaps left by decreased activity of Western banks during the financial crisis.

The EFCC also helped to address the problems in the Niger Delta, which, in my opinion, is driven entirely by corruption. Indeed, one of the governors of the Delta that we investigated offered me $15 million in cash to stop the investigation against him. We charged him both for the theft of state revenues and for the bribery attempt. Sadly today he is still one of the most powerful political figures in both the ruling party and the country. This clearly highlights the problem of the Delta – money meant to have gone for development has gone to very few hands and is used for negative ends. In 2003-4, almost 100,000 barrels of oil was stolen daily; by 2005-6, we had managed to reduce this to 10,000 barrels per day. We also secured convictions for kidnappers in the Delta, who were driving the cycle of violence and bribery with the private oil companies.

The entire team responsible for these successes, which was trained by a variety of agencies in the US, has been moved out of the EFCC. I personally have been dismissed from the service, though I continue to challenge this dismissal in court. After surviving an assassination attempt, I decided to relocate temporarily out of Nigeria. But much work remains to be done.

But the policy today in Nigeria is to use all the right rhetoric – speaking of the need for rule of law and the fight against corruption – to cover-up their real campaign to completely undo the reform efforts of the previous government and so thoroughly confuse corruption and anti-corruption that no one can sort out which is which any longer. This is why today, many of the law enforcement agencies that used to work hand-in-hand with the EFCC are no longer willing to partner with the EFCC or the Nigerian Justice Department. The issue of integrity is paramount in such relationships.

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I offer these examples to illustrate the challenge in fighting corruption. When you fight corruption, it fights back. It will likely have greater resources than you, and it is lead by those who operate outside the law and view the fight as life-and-death for their survival. In a globalized and networked world, we all need to believe that the fight against corruption must assume a transborder dimension. Our own modest success at the EFCC was supported by efforts of institutions of the United Nations, regional bodies, and many bilateral bodies like the US Secret Service, the FBI, the US Postal Service, and the Department of Justice. I would particularly mention the support we got from the United States in setting up and nurturing the Nigeria Financial Intelligence Unit. We were also aided by the emergence of statutes that offered universal applicability. But without a doubt, the fight against corruption in countries like Nigeria will require strengthening international regulations and standards to enable enforcement on the ground.

For example, the work of the EFCC would not have been possible without the Financial Action Task Force, which de facto forced Nigeria to develop new anti-

money laundering laws and spurred the creation of the EFCC. However, the FATF lost its original might and importance and there is a need to strengthen it, empower it, and provide the necessary framework for international financial regulations. Stronger global standards against money laundering can force Nigeria and other countries to accept that the old way of business will come with too high a cost.

Similarly, the US could help promote a Proceeds of Crime law that has treaty status, and push the boundaries of the Foreign Corrupt Practices Act (FCPA) to be expanded power to bite both givers and takers of bribes. Until those receiving the bribes are punished for their actions, the marketplace for high-stakes elite bribery will continue to thrive. I would also propose that Congress support civil society monitoring programmes and direct support for programmes building investigative journalism, which can support transparency and anti-corruption efforts.

Other challenges will include expanding cooperation in intelligence gathering and sharing and reigning in the vicarious liability of tax havens and offshore banks. This comes back to the theme of today's hearing, about the role of financial institutions. Safe havens are undermining the effort of poor nations to make progress and we must all work in concert to ensure that secrecy does not undermine greater transparency and accountability. The UK's Commission for Africa estimates that the assets stolen from the continent and held in foreign bank accounts amount to $93 billion. If Africa can succeed in tracing and repatriating such stolen wealth, the next chapter in the story may truly turn a new page, and the days of aid dependency can start to wane.

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From a distance, systemic corruption seems like too big a hurdle to overcome. Nigeria's problems may seem insurmountable, but the rest of the world can make a difference by doing what they can to promote transparency. In five short years, the EFCC was able to make a difference in one of the most challenging environments on the planet; the lesson is that small measures with limited support can bring about meaningful change.

But to do this, Western partners and others must truly understand how corruption works and that in some instances they have been unwilling partners to it, even when the intentions have been nothing but good. Corruption is often viewed as a political challenge, and many donor nations would rather support more humanitarian-based causes, like health and education. But it is time for everyone to understand that by pumping money into development efforts without a clear accountability mechanism as a part of such programs, these efforts are often as good as putting money down the drain. The US has many new health and development initiatives in Africa – in Nigeria alone the total is over a half billion dollars a year. You owe it to yourselves and to your taxpayers to ask how this money is spent, ask for results, and insist that any such funds are spent to the good of the people. I believe if you looked more closely at some of the organizations in Africa tasked with utilizing these funds, you would not like what you see. The same is true of any nation offering development aid on the continent; the need for greater oversight standards are needed by all partners.

The examples I give today are not to point fingers, but to illustrate that corruption is killing Nigeria, and it is killing across the African continent. I urge you to view the fight against corruption as the ultimate humanitarian effort, for surely there is

no stronger chain to shackle the poor to their lot. Corruption may have taken some shots at us, but what it is doing to ordinary Nigerians every day is far worse and far more fatal.

When corruption is king, there is no accountability of leadership and no trust in authority. Society devolves to the basic units of family and self, to the baser instincts of getting what you can when you can, because you don't believe anything better will ever come along. And when the only horizon is tomorrow, how can you care about the kind of nation you are building for your children and your grandchildren? How can you call on your government to address what ails society and build stronger institutions?

Corruption makes democracy impossible because it subverts the will of the people. A select few, with so much money and authority, continue to steal elections and make a mockery of the notion of government by the people or for the people. Nigeria today is the worst example of electoral theft in the world. So it is also important that the United States and other partners in Nigeria stand by the Nigerian people first and foremost, and say that enough is enough.

Corruption is one of the greatest crimes the world has ever known. But those who are suffering the most from its poison are the least able to fight it; their resources, their health and wellbeing, and their futures have been stolen away. There is no surer salt in the earth of democratic and representative governance. It is for this reason that I call on you to help fight this global injustice, both for the sake of Nigeria, and for every other country that will never know its potential without your support. But at the end of the day it will be we, the Nigerians and

the Africans, that will have to solve our own problems and catch up to the rest of the world in freedom and development. I assure you that can be done.

Thank you once again for this kind invitation and I now welcome your questions.