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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 CURTAIL THE GLOBAL PROBLEM

By Raymond W. Baker
Global Financial Integrity

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 Mobutu, 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 through-

out 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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¹See, 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



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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

²Joly, *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 Glaxo-SmithKline, 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.

³Address 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.

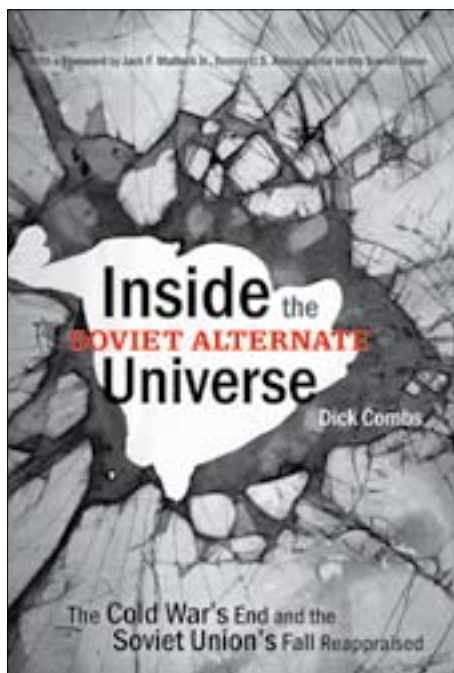
Policy has tended to trail behind galvanizing events. The U.S. Foreign Corrupt Practices Act (FCPA) of 1977 followed both the Watergate scandal, which helped create the right political climate, and a series of investigations revealing that more than 400 corporations had admitted paying \$300 million 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

⁴French 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.



INSIDE THE SOVIET ALTERNATE UNIVERSE
THE COLD WAR'S END AND THE SOVIET UNION'S FALL
REAPPRAISED

Dick Combs

With a foreword by **Jack F. Matlock Jr.**

"I greatly benefited from Dick Combs' deep understanding of Soviet culture and thinking during his service as my U.S. Senate foreign policy advisor. His depth of knowledge and balanced judgment are clearly reflected in this book, which offers fresh, persuasive analysis of the end of the Cold War and the fall of the Soviet Union. Policymakers, academics and the public can draw important foreign policy lessons from Combs' insightful account." —Former U.S. Senator Sam Nunn

"Synthesizing memoir, history, and policy analysis, Dick Combs's book combines an instructive inside account of a high-ranking American diplomat's years in the Soviet Union with a critical analysis of the evolution of Soviet thinking about world affairs. It also analyzes American thinking about the USSR and applies the lessons of all this to understand post-Soviet Russian politics and foreign policy, and American misperceptions thereof." —William Taubman, Amherst College

"Throughout the post-Soviet period, the Nunn-Lugar program has been a primary vehicle through which the new Russian-American relationship has evolved. Dick Combs was one of the original conceptualizers of that program, born of his understanding of the deep-seated social and psychic strains unleashed by the Soviet collapse, but also a major facilitator of the policy's application through his mastery of the Russian language and his appreciation of the sensibilities of the Russian people and their leaders." —Senator Richard Lugar

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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.

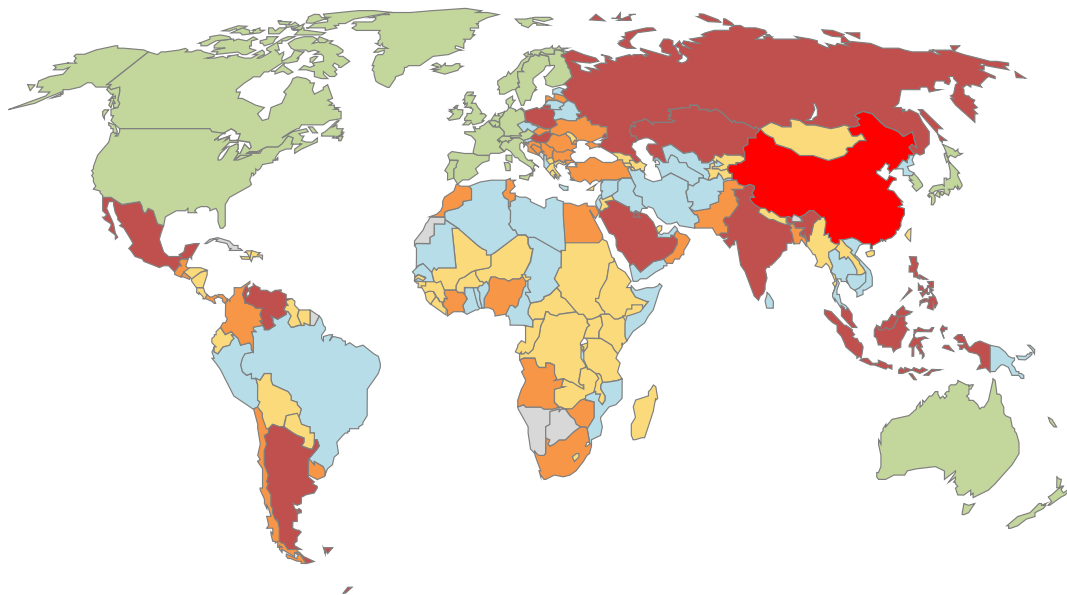
Of course, it won't be easy. Powerful vested interests have a lot to lose from cleaning up the current state of global capitalism. But the rest of us have even more to lose if we don't. If global capitalism cannot be rendered essentially fair, then it is unlikely to be sustainable in a world where formerly 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



Executive Report

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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	2002	2003	2004	2005	2006
(\$millions)	\$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



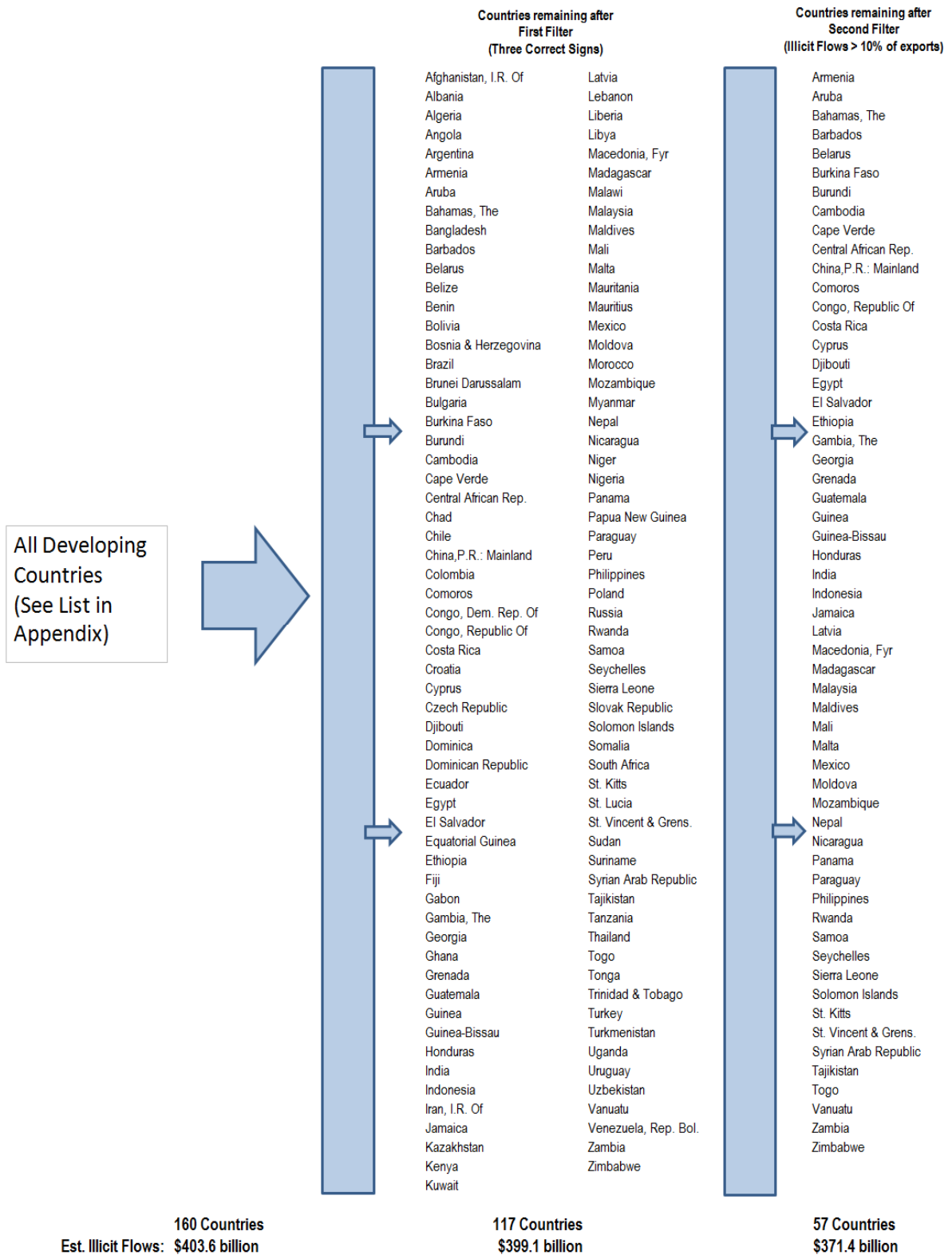
to be less affected by valuation changes than the change in debt stocks, they are more likely to have gaps and be less-up-to-date compared to the CED data. These data issues may explain in general the somewhat lower illicit financial flows estimates based on NDF compared to those based on CED. The main 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.



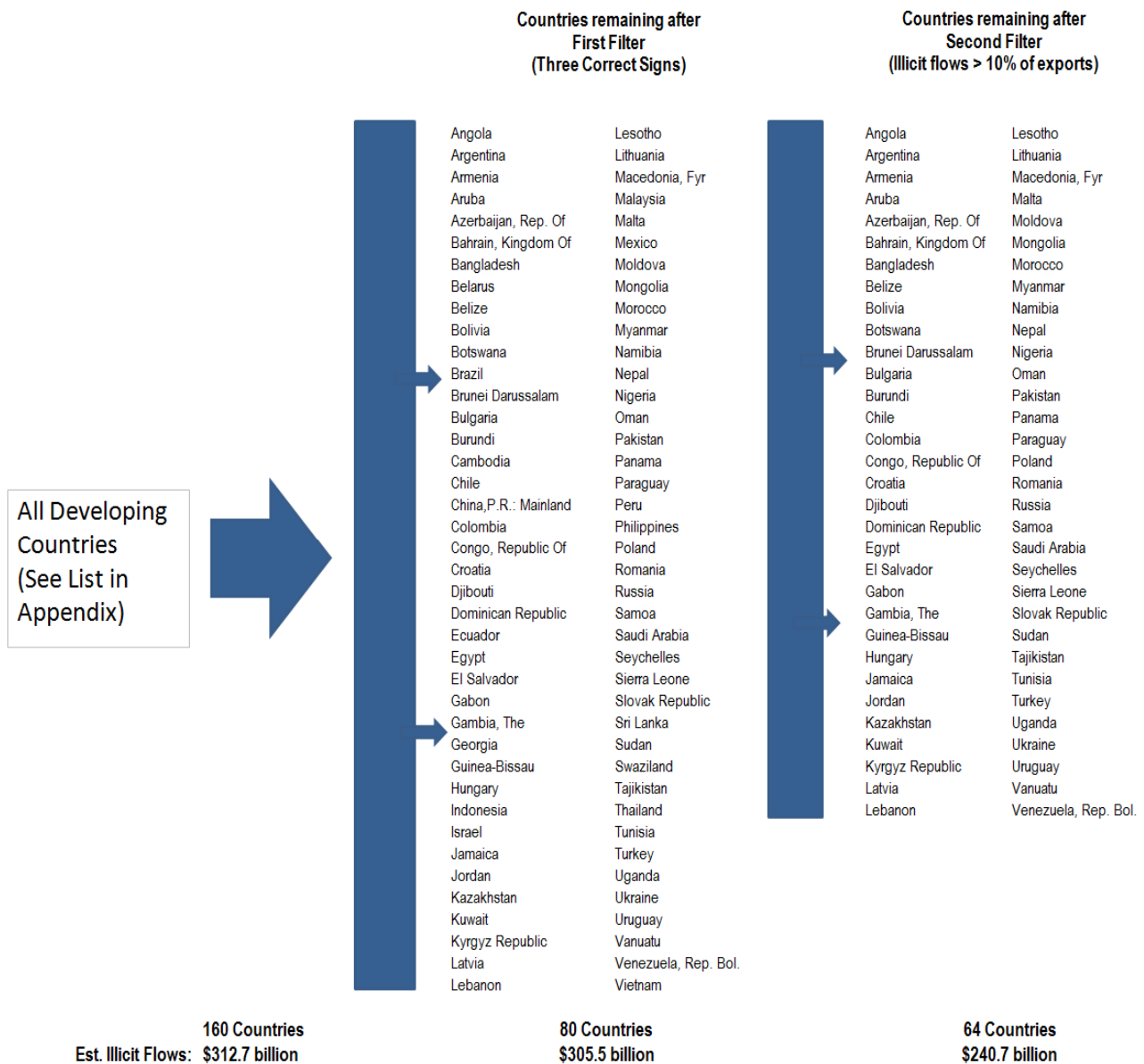
Chart 1. The Two-Stage Filtration Process for GER at 10 percent of Exports f.o.b.: A Schematic Diagram (Average 2002-2006)





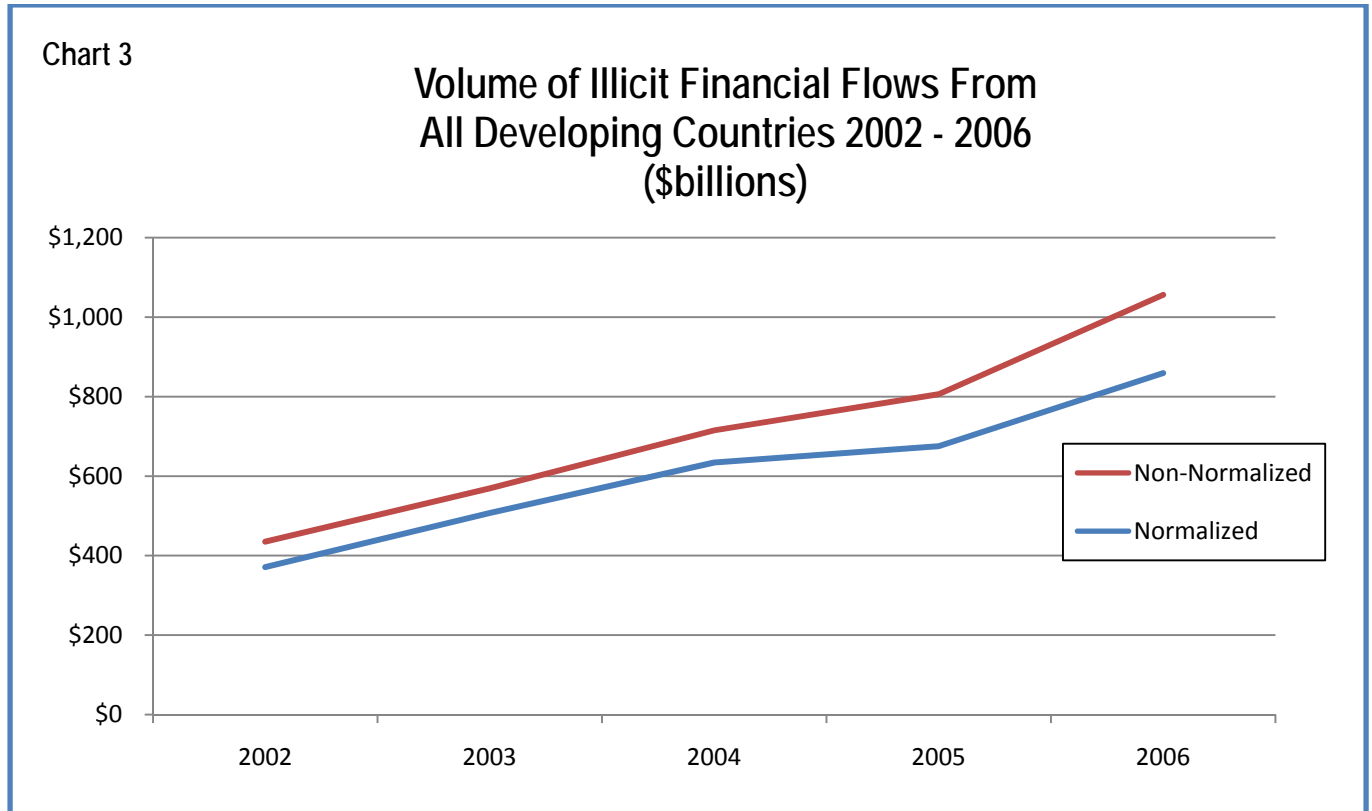
29. Chart 2 depicts a similar two-stage filtration process on average CED estimates of illicit financial flows. The two-stage filtration on CED indicates that on average \$240.7 billion flowed out of developing countries per year over the same period. Normalized estimates provided by the combined GER-CED 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

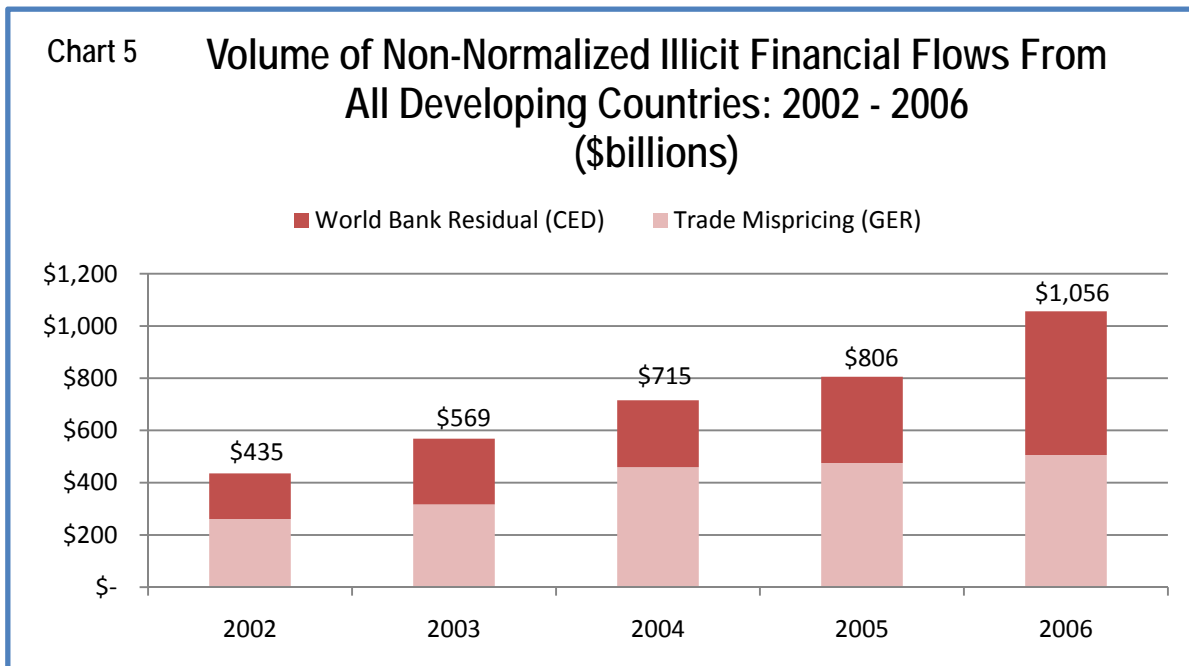
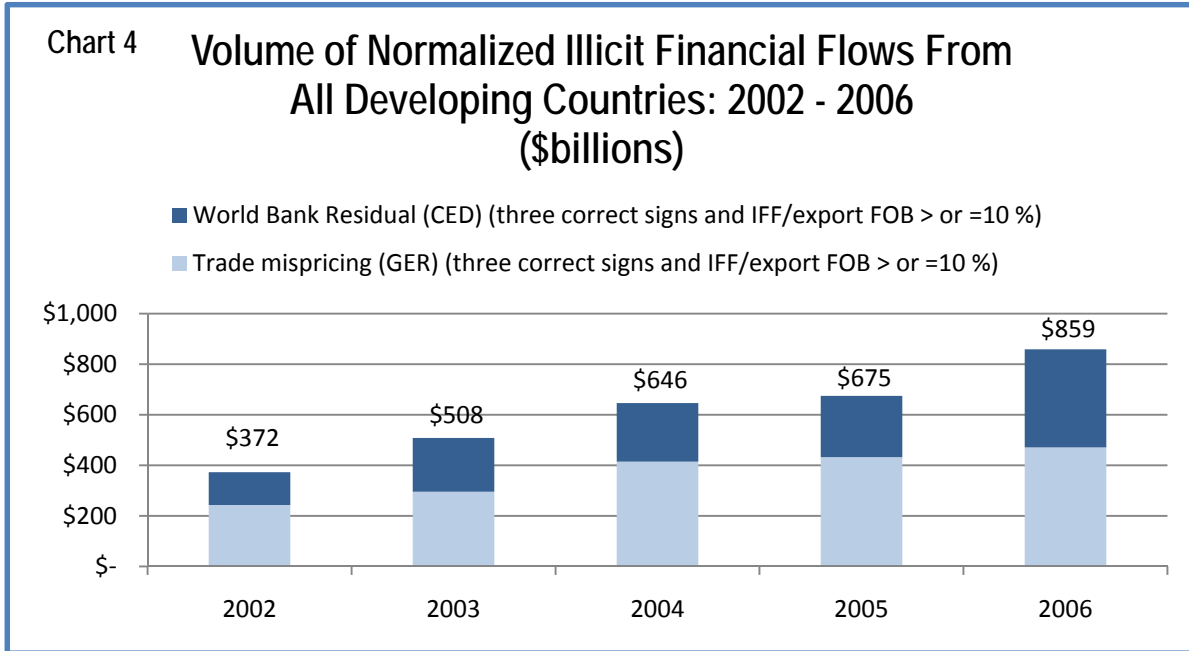


30. In 2006, the last year for which official data are available, the range of illicit financial flows increased to between \$858.6 billion (normalized)—\$1.06 trillion dollars (non-normalized).
31. In 2002, the first year for which data were analyzed for this study, the volume of illicit financial flows 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.



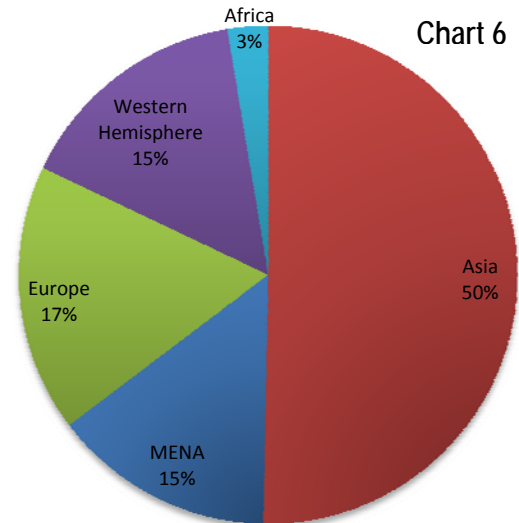
36. Asia accounts for approximately 50 percent of overall illicit financial flows (Charts 6 and 7) from developing countries and normalization of the estimates does not significantly alter this picture. The large volume of illicit outflows from China (mainland) is behind Asia's dominance in overall illicit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

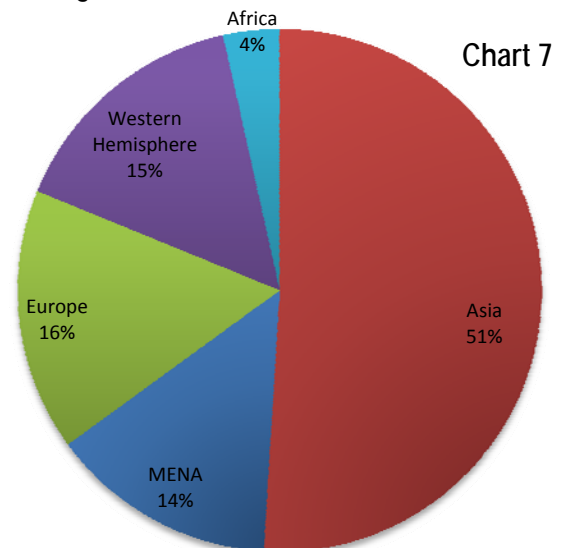
38. A handful of countries in Europe, particularly Russia, are driving Europe's second place (around 16-17 percent) in the share of overall illicit flows from developing countries.

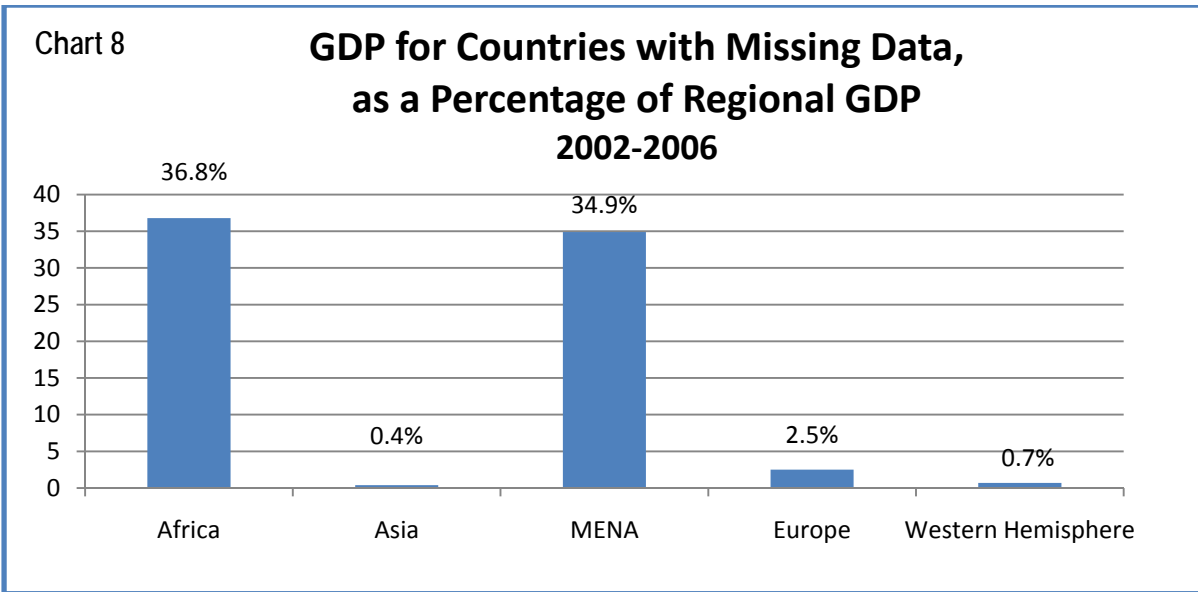
39. By far, the share of illicit flows from Africa is the lowest among all developing regions (approximately 3 percent of the total). **However, there are strong reasons to believe that the share would probably have been higher if more complete and reliable trade and external debt data were available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

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



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





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)

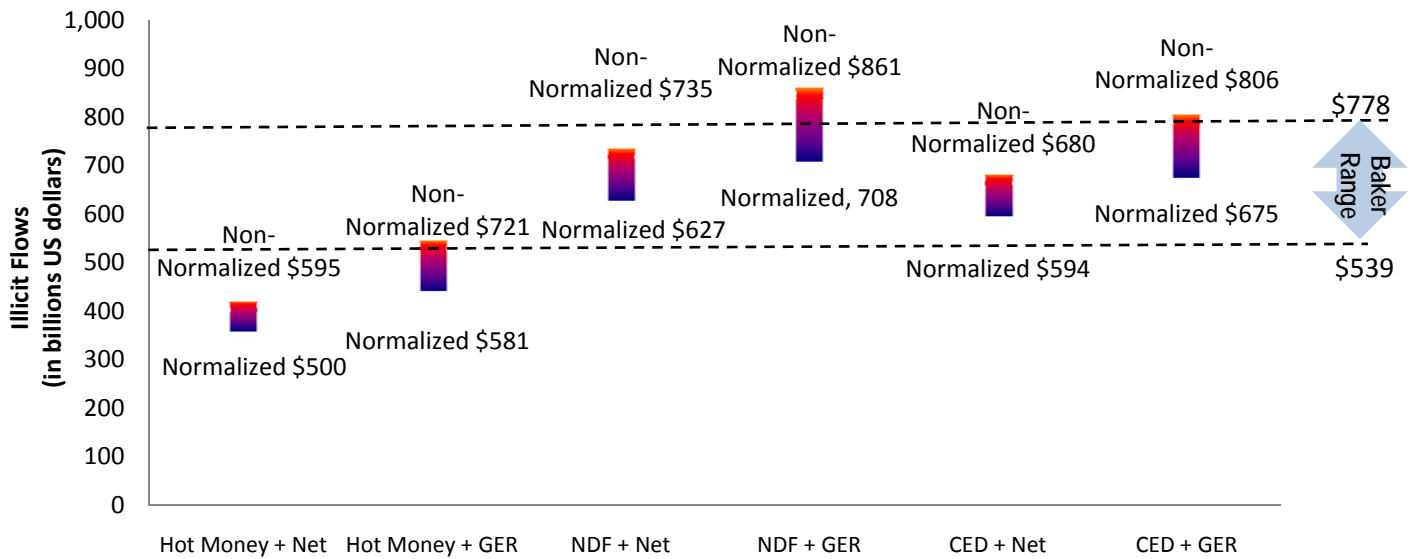
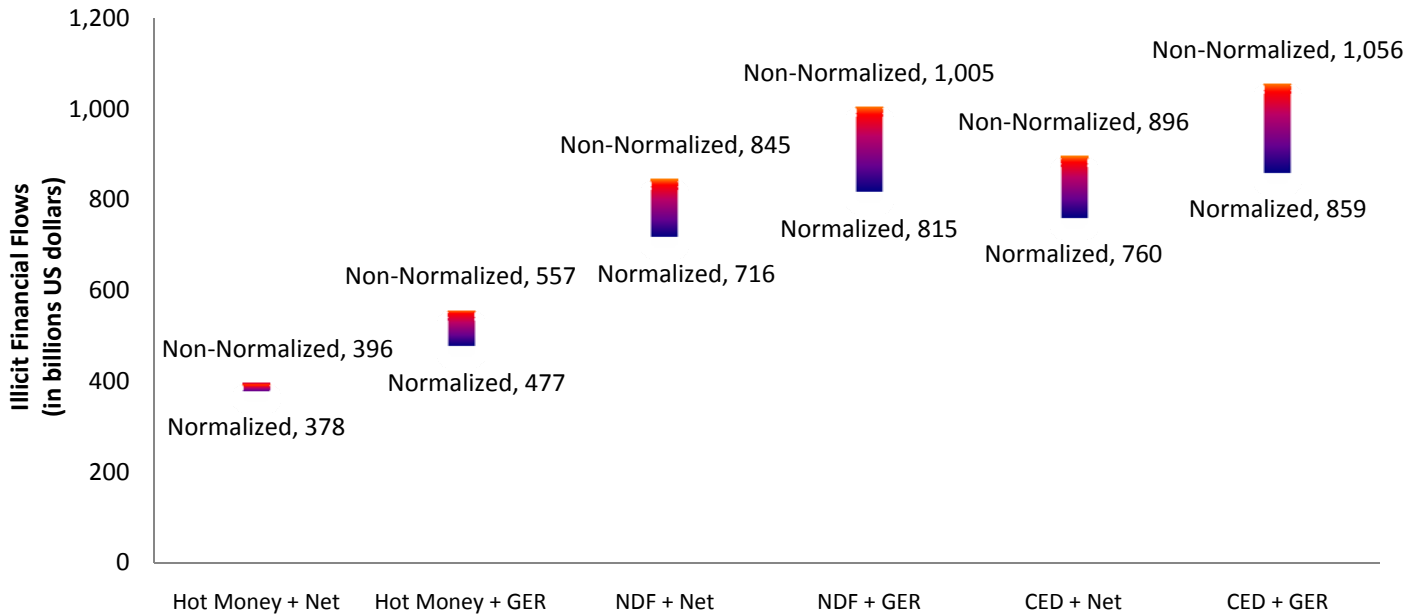


Chart 10

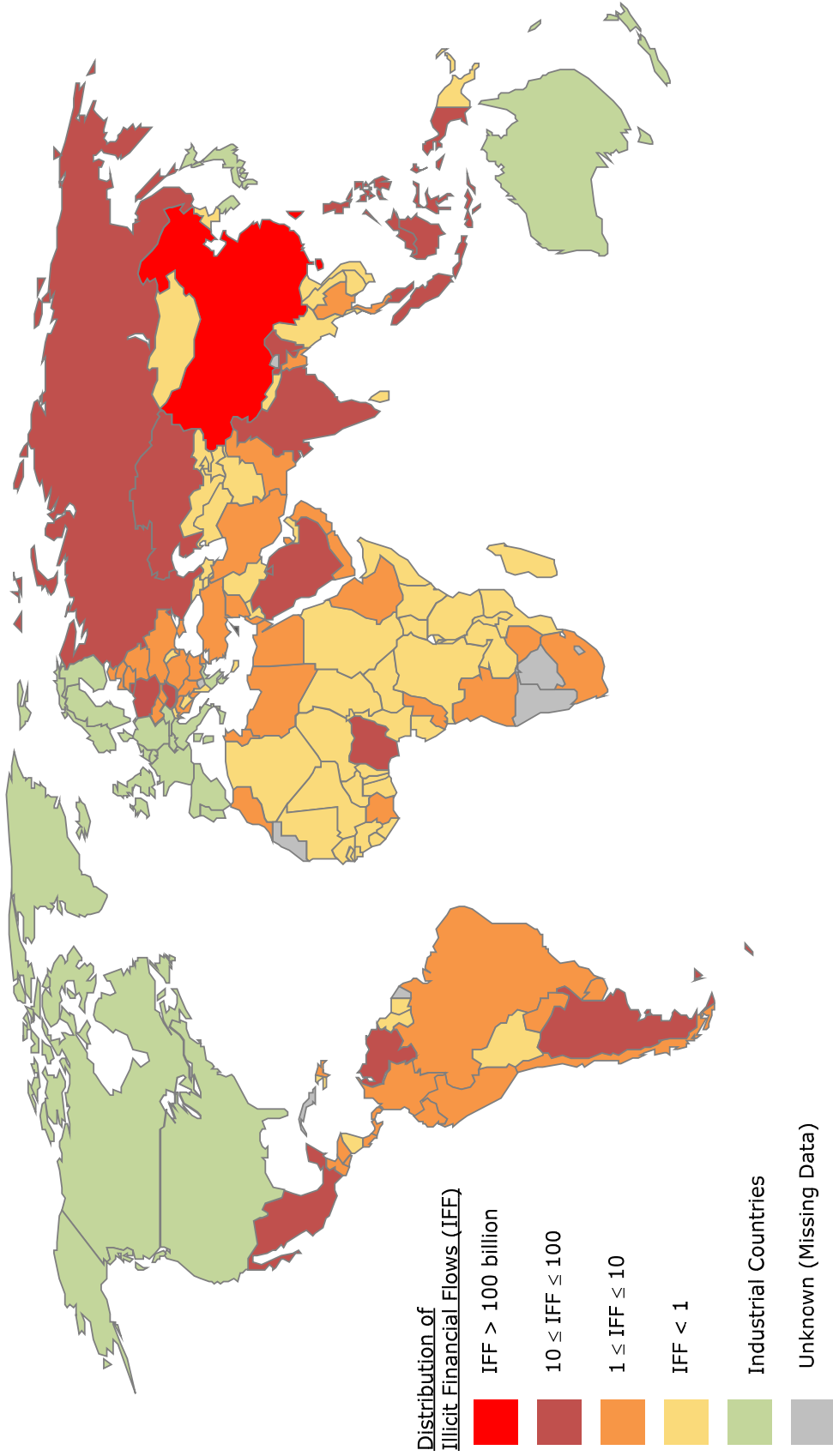
Comparison of Illicit Financial Flows Estimates from Developing Countries
(in billions of U.S. dollars, 2006)





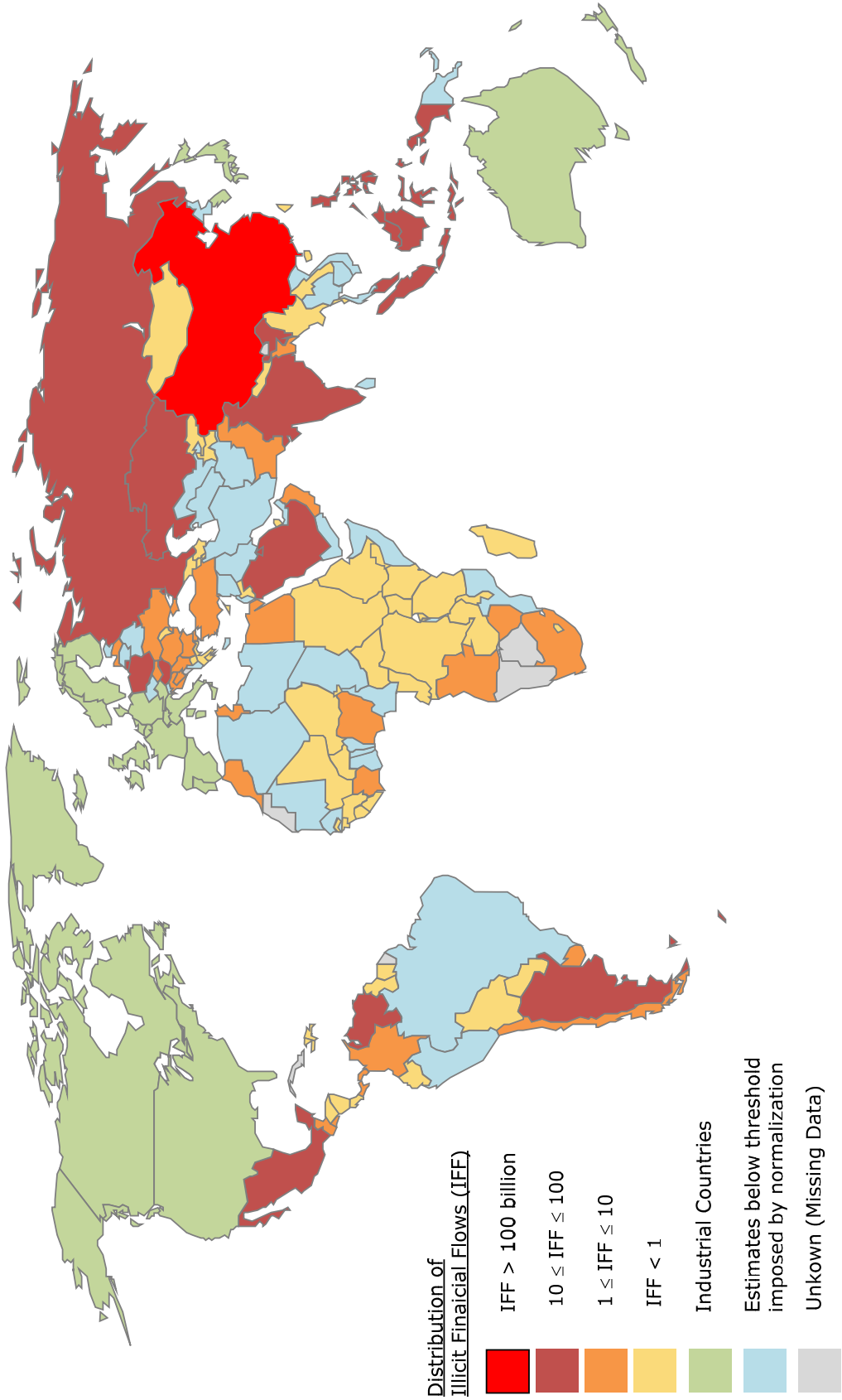
44. The regional dispersion of illicit financial flows discussed above is depicted in two full-page world maps that are color-coded to show the non-normalized and normalized global distribution of illicit financial flows as measured by the CED-GER models.
45. In these maps illicit financial flows from 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 2002-06¹



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 2002-06¹



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

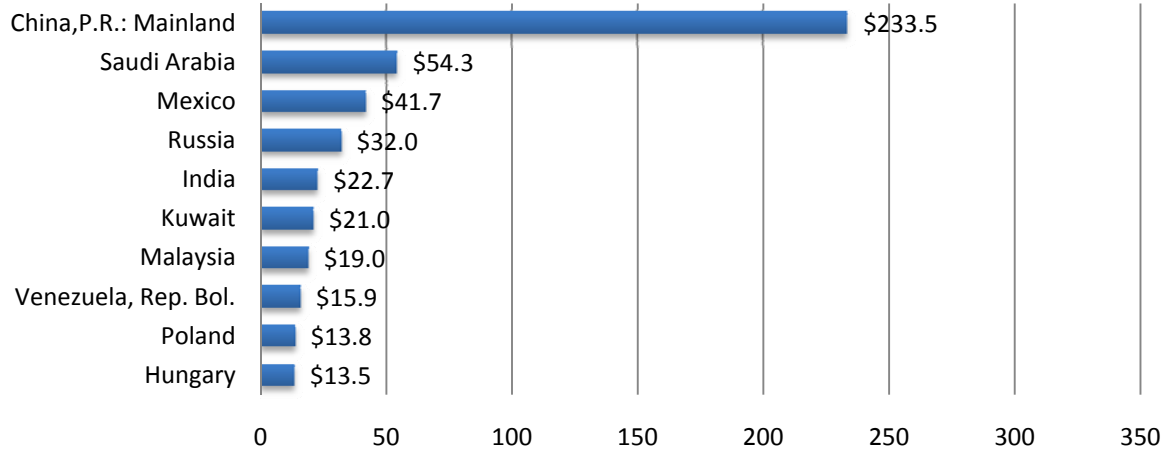
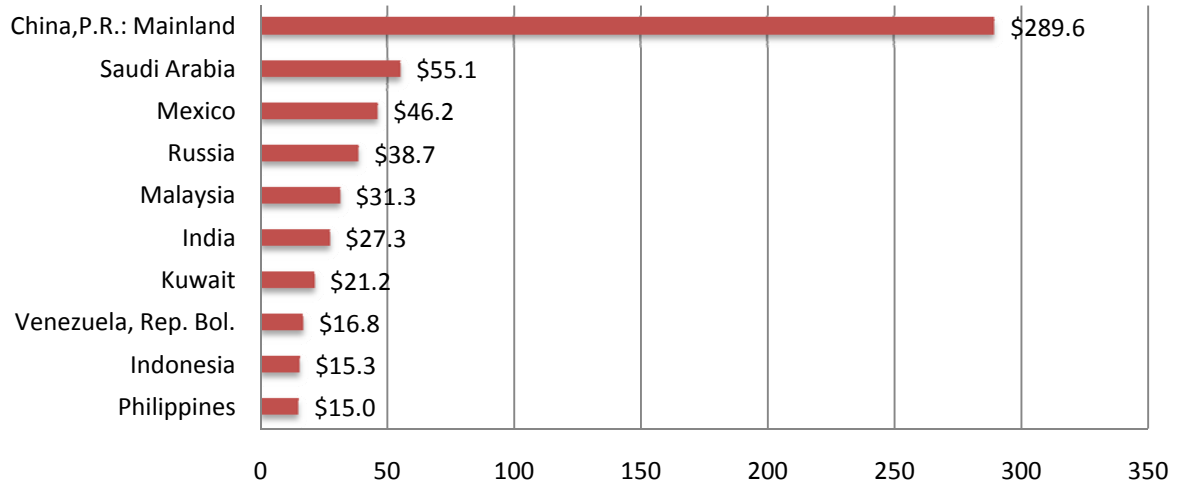


Chart 14

Top Ten Countries with Highest Average Non-Normalized Illicit Financial Flows, 2002 - 2006





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 & Príncipe				
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.

