

**THE WORLD BANK GROUP'S
RESPONSE TO ILLICIT FINANCIAL FLOWS:
A STOCKTAKING**

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Abbreviations and Acronyms

AEOI	Automatic Exchange of Tax Information
AML	Anti-Money Laundering
APEC	Asia-Pacific Economic Cooperation
ASEI	African Sustainable Extractive Industries Facility
CCSI	Columbia Center on Sustainable Investment
ECA	Economic Commission for Africa of the United Nations
EITI	Extractive Industries Transparency Initiative
EOIR	Exchange of Tax Information Requests
FATF	Financial Action Task Force
FfD	Sustainable Development Goals and the Financing for Development
GFI	Global Financial Integrity
GGP	Governance Global Practice
GRP	Good Regulatory Practice
ICHA	International Corruption Hunter's Alliance
IFFS	Illicit Financial Flows
INT	Integrity Vice Presidency
JAAG	Justice At A Glance
JSPEIR	Justice Sector Public Expenditure and Institutional Review
JUSTPAL	Justice Sector Peer Assisted Learning Network
KRA	Kenyan Revenue Authority
ML	Money Laundering
NNPC	Nigerian National Petroleum Cooperation
NRA	National Risk Assessment
NRGI	National Resource Governance Institute
NSWG	National Stakeholders' Working Group
RAS	Reimbursable Advisory Services
RIA	Regulatory Impact Assessment
SCD	Systematic Country Diagnostic
StAR	Stolen Asset Recovery Initiative
TF	Terrorist Financing
UIAF	Columbian Financial Intelligence Unit
UNCAC	UN Convention against Corruption

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1. Introduction

1. The term “Illicit Financial Flows” (IFF) began to appear in the 1990s to describe a number of cross border activities. The term was initially strongly associated with capital flight. It now generally refers to cross-border movement of capital associated with illegal activity or more explicitly, money that is illegally earned, transferred or used that crosses borders. This falls into three main areas:

- The acts themselves are illegal (e.g., corruption, tax evasion); or
- The funds are the results of illegal acts (e.g., smuggling and trafficking in minerals, wildlife, drugs, and people); or
- The funds are used for illegal purposes (e.g., financing of organized crime).

In-depth studies have found that the different types of IFFs are often linked in exchanges and relationships that involve corruption, organized crime, and international commercial fraud.

2. **Global estimates indicate that IFFs are substantial and growing.** IFFs are inherently difficult to measure, given the illegality of the flows and their underlying activities. Global Financial Integrity (GFI) estimates that developing countries lose almost US\$ one trillion per year—a number that is perhaps most usefully seen as suggesting the scale of the phenomenon.¹ The Economic Commission for Africa of the United Nations (ECA) has used trade statistics to estimate that between 2001 and 2010 African countries lost up to US \$407 billion from trade mispricing alone.² While these estimates are difficult to verify (and are not always consistent), they indicate that the amounts involved are significant and pose widespread problems, particularly in resource-rich countries and fragile and conflict-affected states.³ Regardless of the exact numbers, both GFI and ECA estimates show an upward trend for IFFs from 2001 to 2013.

3. **The size and nature of IFFs have important implications for development.** IFFs may directly reduce government revenue and thus reduce resources available for development purposes. IFFs are symptomatic of other issues that constrain poverty reduction and shared prosperity, such as vested interests, and weak transparency and accountability. The activities that underlie IFFs, such as fraud, tax evasion, and illegal exploitation of natural resources are also detrimental to development.

4. **The WBG has recognized the need to tackle the IFF issue.** WBG President Jim Kim has identified IFFs as an important challenge to achieving the World Bank Group’s twin objectives of eliminating extreme poverty and boosting shared prosperity. The World Bank Group’s approach to IFFs emphasizes the importance of addressing the illicit flows themselves, as well as the underlying activities. The WBG effort is designed to create a strong coalition of forces, working

¹ GFI (2014) Illicit Financial Flows from Developing Countries: 2003-2012. <http://www.gfintegrity.org/report/2014-global-report-illicit-financial-flows-from-developing-countries-2003-2012/>. See Illicit Financial Flows: The Most Damaging Economic Condition Facing the Developing World, GFI, Sept 2015, for GFI’s recent analysis on the quantum of illicit flows and their impact.

² African Union & Economic Commission for Africa (2015) Report of the High Level Panel on Illicit Financial Flows from Africa.

³ AfDB, ADB, EBRD, EIB, IDB, IMF, & WBG (2015) From Billions to Trillions: Transforming Development Finance. Post-2015 Financing for Development: Multilateral Development Finance.

on a variety of platforms, to prevent illegal activities from occurring and illegal funds from being transferred internationally.⁴

5. This paper documents WBG experience and proposes the future direction of its work on IFFs. In order to inform future work on IFFs, this note defines IFFs and sets out WBG experience working on them to date. Also, it presents some areas for future activities to take up this challenge.

1.1 Defining IFFs

6. While there is now a growing degree of familiarity with the term “illicit financial flows,” there is still no global consensus on its definition. The Report on the High-Level Panel on Illicit Financial Flows from Africa (“the Mbeki Report”) adopted the definition used by Global Financial Integrity (GFI), where IFFs are defined as “cross-border movement of money illegally earned, transferred or used.” The High-Level Panel and GFI divide IFFs into three categories based on the source of the flow: (i) corruption; (ii) criminal activities; and (iii) commercial activities.

7. There is an ongoing debate on which commercial activities should be considered as part of IFFs. What constitutes IFFs within the context of international trade, especially in relation to tax avoidance and tax fraud, is still being debated. For example, tax can be avoided through activities such as legal tax planning and optimization. This is different than IFFs that arise through the fraudulent mispricing of goods traded between independent parties, illegal transfer pricing within a multi-national corporation, or fictitious transactions.

8. The WBG understands the term “IFFs” to cover both the flow of illicit funds and assets across borders and the underlying activities that generate the flows. Money and activities that have a clear connection with illegality – corruption, illegal natural resource exploitation, smuggling and trafficking, money laundering, tax evasion and fraud in international trade – fall under IFFs. Tax avoidance activities, such as legal tax planning and optimization, do not belong to IFFs.⁵ The WBG is committed to addressing the tax avoidance issue, and this is dealt with primarily through the WBG’s work on international tax policy and domestic resource mobilization.⁶ The principle adopted by the WBG is that cross-border movement of financial assets are considered illicit only when they are associated with activities that are deemed to be illegal in the local jurisdiction.⁷

⁴ For the best discussion of the nature of IFFs and strategies for addressing IFFs, see Reuter, Peter, eds., *Draining Development: Controlling Flows of Illicit Funds from Developing Countries*, World Bank, 2012.

⁵ The clarity of these distinctions is easier to maintain conceptually than in real life. For example, should the calculation of IFFs in a country include the full value of a tax holiday for an international firm obtained through corrupt means? The vagueness around the precise boundaries of what counts as an illicit flow reflect the nascent character of the IFF agenda and emphasizes the need to establish coherent approaches to problems that may straddle current boundaries.

⁶ AfDB, ADB, EBRD, EIB, IDB, IMF, & WBG (2015) *From Billions to Trillions: Transforming Development Finance. Post-2015 Financing for Development: Multilateral Development Finance*
[http://siteresources.worldbank.org/DEVCOMMINT/Documentation/23659446/DC20150002\(E\)FinancingforDevelopment.pdf](http://siteresources.worldbank.org/DEVCOMMINT/Documentation/23659446/DC20150002(E)FinancingforDevelopment.pdf)

⁷ The degree of opaqueness in determining the precise borders of IFFs are due, in part, by the nature of tax crimes. In many cases, whether a firm’s tax behavior amounts to legal tax avoidance or illegal tax evasion can only be determined after the fact based upon a legal ruling.

9. **Recent international attention on IFFs has generated a demand for action that is in many ways far ahead of the analytical work and understanding of the issue.** For example, there is no agreed-upon way of bringing together information on illicit outflows and illicit inflows to calculate the volume of IFFs in a given country.⁸ Analysis and policy work by the WBG and others can help provide policy makers with accurate information and a clear understanding of the phenomenon so as to better align actions.

1.2 IFFs and Development

10. **Illicit Financial Flows have an adverse impact on development.** IFFs are a symptom of problems that institutionalize inequality and constrain prosperity. Factors that foster illicit practices and illegal international movement of capital include: policy and regulatory inconstancies; weak institutions; limited oversight, accountability and rule of law; entrenched vested interests; and the absence of transparent economic and governance processes. Addressing the causes of IFFs and restricting the illicit movement of capital out of developing countries undoubtedly support economic development and growth.

11. **The activities underlying illicit flows are detrimental to development.** Corruption, organized crime, illegal exploitation of natural resources, fraud in international trade and tax evasion are as harmful as the diversion of money from public priorities. Illegal logging, fishing and mineral extraction are strongly connected with deforestation, the depletion of fishing stocks and environmental degradation as well as the impoverishment of individuals and communities who rely on those resources to sustain their existence. Drugs counterfeiting can have even more dire consequences, such as the thousands of preventable deaths from malaria and tuberculosis due to sub-standard counterfeit drugs.⁹ The *World Development Report (2011): Conflict, Security, and Development* demonstrated how global threats – transnational organized crime, corruption, illegal trade in natural resources, the laundering of the proceeds of crime and tax evasion – impact governance and development outcomes across the developing world. These threats fuel grievances and violence, and undermine the effectiveness of national institutions and social norms, ultimately compromising economic growth. There are needless deaths and destructions, and inadequate and poor public service delivery due to illegal movement of funds out of developing countries.

12. **The impact on development is often most acute in the poorest countries—those already struggling to put in place policies, organizations and practices that are essential for stability and prosperity.** The revenue lost to IFFs shrinks private investment and constrains the public resources available for investment and service delivery. This results in inequality in both

⁸ Ongoing work by the IMF on measuring IFFs at a regional level proposes that outflows be subtracted from inflows to determine net IFF. Calculations by GFI and others of IFFs within countries and at the international level have often only considered outflows. Evidence of the developmental harm associated with both inflows and outflows and the activities associated with the flows suggest that adding them together might be most appropriate in order to gauge developmental impact.

⁹ According to the World Economic Forum, sub-standard malaria medicines were responsible for the deaths of over 100,000 children in sub-Saharan countries. The global numbers associated with counterfeit malaria and tuberculosis medicines are significantly higher. See World Economic Forum, Briefing Paper: State of the Illicit Economy, 2015.

opportunities and development outcomes.¹⁰ Developed countries are becoming increasingly aware of the negative costs and consequences of being safe havens for such illegal assets. They recognize that IFFs present significant challenges to development, and, therefore, to development assistance.

13. In view of the adverse impact of IFFs on development, there is a broad consensus among the international community to take action. Overall, IFFs together with the underlying activities distort economic and political competition, subvert government institutions, generate conflict and violence, and undermine the integrity of legal and financial systems. The international community is thus committed to tackling the issue. This is reflected in specific commitments to reduce the flows and increase the return of stolen assets within the United Nations' Sustainable Development Goals and the Financing for Development (FfD) outcomes (See Box 1). Global agreements to tackle IFFs also reinforce commitments made at the regional level by African heads of state and other forums.¹¹ Currently, commitments relating to stopping IFFs rely on international legal agreements and standards such as the UN Convention on Transnational Organized Crime, UN Convention against Corruption, OECD Anti-Bribery Convention, Global Forum on Transparency for Exchange of Tax Information and the Financial Action Task Force (FATF).

Box 1: IFFs in Sustainable Development Goals and Financing for Development Outcome Documents¹²

SDGs: Sustainable Development Goal 16 is to: “Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels.” Target 16.4 sets the expectation by 2030 to “significantly reduce illicit financial and arms flows, strengthen the recovery and return of stolen assets and combat all forms of organized crime.” Other targets to support Goal 16 address the rule of law; corruption and bribery; institutions and governance; and violence, terrorism and crime.

The Financing for Development commitment on IFFs is to “substantially reduce and eventually eliminate IFFs” by i) combatting tax evasion and corruption through strengthened national regulation and increased international cooperation; ii) reducing opportunities for tax avoidance; and iii) enhancing disclosure practices and transparency in both source and destination countries, e.g. through transparency in financial transactions between governments and companies to relevant tax authorities.

14. Reducing IFFs represents an enormous challenge which can only be achieved through a concerted and coordinated global effort. While the foundations for an effective action already exist, taking them to a scale with greater impact will require a different level of collaboration among developed and developing countries, as well as between state and non-state actors at local, national, and regional levels. A comprehensive engagement by the international community will stretch from strengthening financial regulations and enforcing anti-money laundering rules, to combating organized crime, all the way to enhancing border controls and tracking revenues related to mineral extraction. It will need to ensure that policies designed to stop IFFs do not have unintended consequences, such as creating barriers for remittances or reducing access to banking

¹⁰ It is important to note that some activities, such as low-level cross-border shadow trade in food stuffs and other simple commodities, may not generate negative economic or development consequences. Policy responses to IFFs need to be informed by information on the developmental impact of the different activities that fuel illicit fund flows.

¹¹ African Union & Economic Commission for Africa (2015) Report of the High-Level Panel on Illicit Financial Flows from Africa. http://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf

¹² UN (2015) The Addis Ababa Action Agenda of the Third International Conference on Financing for Development. <http://www.un.org/esa/ffd/ffd3/wp-content/uploads/sites/2/2015/07/Addis-Ababa-Action-Agenda-Draft-Outcome-Document-7-July-2015.pdf>. UN (2015) Transforming our world: the 2030 Agenda for Sustainable Development. http://www.un.org/ga/search/view_doc.asp?symbol=A/RES/70/1&Lang=E

services among poorer communities.¹³ No single actor has the scale and scope to be effective across the entire breadth of engagements but it is vital for each party to identify what it is doing on the issue and to determine how it can best contribute going forward.

15. Strategies for tackling Illicit Financial Flows include stopping the flows and preventing the underlying activities. A running debate exists regarding strategies for stopping IFFs. Some commentators and organizations have emphasized strategies that are exclusively focused on strengthening financial oversight, preventing outflows and inflows of capital assets, and returning stolen assets. These strategies often work to increase the power and authority of financial regulators and law enforcement officials. Such approaches emphasize a common strategy for all IFFs regardless of their origin or what countries and sectors are involved. Experience with the enforcement of anti-money laundering rules and enhanced financial regulation has demonstrated the power of these approaches, as well as their limitations.¹⁴ Work in the anti-corruption arena has also demonstrated the importance of a balanced approach that includes institutional strengthening since increasing the power and authority of law enforcement agencies in countries with weak governance sometimes yields mixed results and does not always promote the rule of law.¹⁵

2. WBG Engagements on IFF

16. The WBG has past and on-going engagements in the area of IFFs. The WBG has substantial experience working on anti-money laundering and asset recovery. It has an extensive portfolio of efforts to help clients design and implement reforms that address the activities that generate illegal revenues. Those engagements encompass assistance to clients in strengthening accountability and governance to support improved management, control, and oversight of specific activities. Core engagements include support for anti-corruption efforts and improved auditing, and assistance on policies relating to the transparency of public finance, tax evasion, public procurement, trade facilitation and border crossing, natural resource management and economic regulation.

17. WBG efforts are organized around three streams of work that are the foundation of responding to IFFs: measuring illicit flows; assisting client countries in preventing the underlying behaviors that give rise to illicit funds; and supporting country and international efforts to stop the flow of illicit funds and recover stolen assets. WBG support is being provided through various channels, including lending and advisory services, convening, and contributing knowledge on several topics that are directly relevant to tackling IFF. (See Table 1). Recently, the WBG is beginning to link analysis and activities using a common IFF perspective.

¹³ The WBG already has experience developing safe corridors for remittances, based upon past work in countries such as Somalia.

¹⁴ For a discussion of the experience of applying anti-money laundering regulations in developed countries, see Levi, Michael, "How Well do Anti-Money Laundering Controls Work in Developing Countries," in Reuter, Peter, ed, *Draining Development: Controlling Flows of Illicit Funds from Developing Countries*, World Bank, 2012, chapter 12.

¹⁵ See Huther, Jeff and A. Shah, "Anti-Corruption Policies and Programs: A Framework for Evaluation," World Bank Policy Research Working Paper Series, No. 2501, 2000 for a discussion of differences in anti-corruption strategies.

2.1 Measuring IFFs

18. **The critical first step in responding to Illicit Financial Flows is to make the flows visible.** Illicit financial flows are cloaked in the vast stream of capital movement. They are derived from corrupt and fraudulent activities or within the depths of criminal undertakings. Their obscurity has frequently served to mask their combined significance, allowing illegal activity to flourish and do long-term harm to local, regional, and even the global economy.

Table 1: World Bank Group engagements relating to Illicit Financial Flows

Objective: Measuring IFFs at country or regional levels	
Country, regional, global and sectoral studies	Finance and Markets GP; DEC; Governance GP
Objective: Preventing behaviors that give rise to Illicit Financial Flows	
Tax evasion and abusive transfer pricing	Governance GP; Macro GP; Finance and Markets GP; INT
Extractives and natural resources integrity	Energy and Extractives GP; Environment and Natural Resources GP; Governance GP; IFC.
Trade policies, economic regulation, customs and border crossings	Trade and Competitiveness GP; Governance GP; Environment and Natural Resources GP; Finance and Markets GP
Anti-Corruption (including strengthening judicial institutions and support for law enforcement)	Governance GP; INT; Finance and Markets GP; IFC
Objective: Stopping Illicit Financial Flows	
Anti-Money Laundering	Finance and Markets GP, StAR
Stolen Asset Recovery	StAR

19. **Specific studies at a country or regional level have established methodologies for measuring IFFs and provided details at the individual country level.** WBG experts have undertaken country and regional studies on activities that give rise to illicit fund flows which have expanded our information base and created the foundation for more comprehensive methodologies for determining the size and composition of IFFs in a given jurisdiction. Country and regional studies on the sources, dimensions, and dynamics of illicit activities include studies on Malawi and Namibia,¹⁶ Somalia,¹⁷ the money trail from piracy off the Horn of Africa¹⁸; and asset laundering in Colombia.¹⁹ (See Box 2.) Detailed examinations in Tunisia, for example, have tracked the costs associated with the capture of the economy by the Ben Ali family,²⁰ the extent

¹⁶ Yikoma, Stuart, B. Slot, M. Geller, B. Hansen, and F. el Kadiri, *Ill-gotten Money and the Economy: Experiences from Malawi and Namibia*, World Bank, 2011

¹⁷ World Bank, *The Pirates of Somalia: Ending the Threat, Rebuilding a Nation*, African Vice Presidency, World Bank, 2013

¹⁸ World Bank, *Pirate Trails: Tracking the Illicit Financial Flows from Pirate Activities off the Horn of Africa*, 2013

¹⁹ Villa, Edgar, M. Misas, and N. Loayza, "Illicit Activity and Money Laundering from an Economic Growth Perspective: A Model and Application to Colombia," World Bank Policy Research Paper Series, No. 7578, 2016.

²⁰ Rijkers, Bob, C. Freund, and A. Nucifora, "All in the Family: Evidence on State Capture in Tunisia," World Bank Policy Research Working Paper Series, No. 6810, 2014.

and value of tax evasion,²¹ and the volume and composition of illicit trade.²² These studies contribute to an already existing body of knowledge on illicit and illegal activities, such as the substantial literature on the size of shadow economies, the frequency and cost of corruption, and the value of illicit natural resource extraction.²³ These studies have taken an important step in elaborating the monetary value of the problem as well as the developmental consequences of IFFs generated by different types of underlying activities. Much of the work on measuring IFFs has been done in partnership with organizations such as the IMF and the OECD.

Box 2: Example: Measuring IFFs in Colombia

“An Economic Growth Model with Asset Laundering: Evidence from Colombia” provides a rigorous analysis of asset laundering relating to drug trafficking in Colombia. The study was undertaken by the WBG, in partnership with the Colombian Financial Intelligence Unit (UIAF). The methodology, used in combination with anti-money laundering systems and mutual evaluation reports, aims to enable policy makers to estimate existing levels of money laundering and predicate the impact of policy choices on the value of money laundering. The paper contributes to the economic analysis of asset laundering from two perspectives. First, it presents a theoretical model of long-run growth that considers all elements involved (illegal workers, activities, and income, as well as the legal private sector and government). Second, it estimates the size of illegal income as well as the size of asset laundering in the Colombian economy.

20. **In addition, the WBG has undertaken broad efforts to increase the availability of information needed for clients and others to better measure and capture IFF streams.** This work includes increasing information on payments made and received in the extractive sector, to strengthening the ability of clients to identify the final owners of firms, to on-going research on the amount of oil that Daesh is producing.²⁴ Complementary engagements help build capacity to make use of new information flows, such as the support provided to tax authorities and law enforcement officials on getting value from new information regarding tax payments and the assets of public officials. These efforts represent the point where information gathering and action come together.

2.2 Preventing the Behaviors That Give Rise to Illicit Flows

21. **In responding to the needs of its clients, the WBG has built expertise and experience in advising countries on how to prevent many of the activities that give rise to IFFs.** WBG engagements have assisted countries in preventing the specific activities that give rise to IFFs, as well as helped to strengthen oversight and accountability. The WBG provides technical assistance and helps build client capacity to:

- identify tax evasion, especially relating to illegal transfer pricing;
- strengthen the management of natural resources, with a focus on extractive industries;

²¹ Rijkers, Bob, H. Arouri, and L. Baghdadi, To Evade or to Avoid? Political Connections and Taxation in Tunisia, forthcoming.

²² Rijkers, Bob, G. Raballand, and L. Baghdadi, “Political Connections and Tariff Evasion: Evidence from Tunisia” World Bank Policy Research Working Paper Series, No. 7336, 2015.

²³ For example, a recent study by Global Witness, estimated that the value of the illicit jade trade in Myanmar at \$31 billion, or approximately half the size of the entire official economy. See Global Witness (2015) Jade: Myanmar’s “Big State Secret.”

²⁴ Do, Toan, J. Shapiro, C. Elvidge, M. Abdel-Jelil, K. Baugh, J. Hansen-Lewis, and M. Zhizhin, “How much oil does Daesh produce? Evidence from remote sensing,” World Bank Policy Research Working Paper Series, forthcoming, 2016.

- improve customs and border control; and
- fight corruption.

These efforts, which span our developmental and fiduciary streams, encompass undertaking institutional due diligence of potential investment partners and assessments of the risks of illegitimate financial transactions in projects supported by the WBG. Across these engagements, the WBG undertakes a broad range of activities to support the ability of clients to identify, plan, and manage the implementation of reforms that are directly relevant to tackling IFFs.²⁵

2.2a Tax Evasion and Abusive Transfer Pricing

22. **Within its overall program of support for improved tax administration, the WBG strengthens national capacity to prevent tax evasion.** This effort happens along four primary dimensions: (i) support on preventing abusive transfer pricing; (ii) technical assistance to countries to enable them to meet the standards of the Global Forum on Transparency and Exchange of Information for Tax Purposes; (iii) assistance to countries to enable them to participate and benefit from the Automatic Exchange of Tax Information; and (iv) capacity building among law enforcement officials to enable them to identify and sanction tax evasion.

23. **Efforts in relation to transfer pricing offer support for developing countries to adopt and effectively implement transfer pricing rules in accordance with international principles through review of legislation, risk assessments and advice on implementation and transfer pricing audits.** The World Bank supports multi-year engagements in this area, building upon a demonstrated track record of impact. In Colombia, the team’s technical assistance in helping national authorities strengthen practices and oversight of transfer pricing yielded an increase in tax revenues related to transfer pricing by 76% in a single year, and led to the passage of improved transfer price legislation. In Ghana, WBG assistance helped in the drafting of new pricing regulations, and the creation of a dedicated transfer pricing audit group with 19 full-time staff. Program results have been equally robust in Kenya, Rwanda, and Vietnam—increasing tax revenues, improving regulations, and enabling tax authorities to effectively challenge transfer pricing that illicitly shields revenues from taxation. (See Box 3). The Energy and Extractives, Governance, and Trade and Competitiveness Global Practices are working together on a tool kit to map and assess risks in transfer pricing in resource-rich countries and profit shifting to more favorable tax jurisdictions.

Box 3: Example – Combating Transfer Pricing in Kenya

Starting in 2012, the WBG has worked with the Government of Kenya to build capacity within the Kenya Revenue Authority to identify and prevent illegal transfer pricing. The capacity building program is specifically tailored to Kenya’s needs and the auditor’s level of knowledge. Thirty-five staff have been trained on advanced transfer pricing issues, 19 of which are working exclusively on transfer pricing audits. The skills building program has resulted in more efficient work of the Kenyan Revenue Authority (KRA) leading to an increase in the number of audit cases completed, revenue collected, and number of cases going to dispute resolution. More specifically, in a recent case, the KRA successfully negotiated a transfer pricing adjustment based on advice given by the program, which resulted in additional tax revenue of US\$ 12.9 million.

²⁵ The list of specific elements of relevant World Bank Group support includes: analysis; creation of analytical tools; setting and implementation of national strategies and action plans; policy formulation; institutional strengthening; capacity-building, monitoring and evaluation; setting of international standards and commitments; and cooperation and collaboration among governments, international partners, civil society, and the private sector.

24. **Another dimension of WBG assistance is support to client countries to meet the standards of the Global Forum on Transparency and Exchange of Information for Tax Purposes (“the Global Forum”).** This work has been prompted by a recognition that many developing countries are unable to participate in discussions of international tax policy or benefit from mechanisms for collaboration among tax authorities due to capacity issues or policy inconsistencies. (See Box 4.) Over the years, WBG assistance has proved instrumental in enabling countries to become part of the global movement to enhance tax transparency. A partial list of countries that have benefited from the WBG’s technical support includes: Burkina Faso, Cote d’Ivoire, Mauritania, Niger, Nigeria, Pakistan, Papua New Guinea, Tanzania, and Uganda. The WBG has partnered with others to establish the African Initiative—an effort specifically designed to assist in the exchange of tax information.

Box 4: The Global Forum on Transparency and Exchange of Information for Tax Purposes

The Global Forum was established by the OECD in 2000 to establish clear standards for the sharing of information necessary for effective enforcement of tax rules across national boundaries. The Forum was substantially restructured in 2009 at the request of the G20 in order to broaden its membership and strengthen the implementation of standards. The Forum currently has 131 members and is the preeminent body for creating and monitoring the application of international standards related to the exchange of tax information requests (EOIR) and the Automatic Exchange of Information (AEOI).

The Forum’s work includes a rigorous peer review process of regulatory compliance with the standards, as well as a review of actual information practices. Countries found to be lagging in their implementation of standards can be listed as partially or non-compliant, which can carry serious consequences for commercial activities. The WBG’s Offshore Financial Center Policy, for example, uses the peer review classification to determine whether a transaction involving an intermediate jurisdiction is permissible.²⁶

In recent years, the Global Forum has worked more closely with other international bodies such as the Financial Action Task Force (FATF), the preeminent international body on anti-money laundering, on issues that cut across tax evasion and money laundering. Recent progress on the standards to be applied in regard to revealing the true owners of a firm has established greater consistency and coherence in the international framework of direct relevance to combating IFFs.

25. **A special stream of WBG work supports developing countries to participate in the Automatic Exchange of Tax Information (AEOI).** Standards developed by the Global Forum increasingly emphasize the automatic exchange of tax information—systematic and periodic transmission of “bulk” taxpayer information by the source country to the residence country concerning various categories of income—as a key element of efforts to combat tax evasion. These exchanges pose few technical problems for tax authorities in developed countries working within fully electronic systems, but can be overwhelming for officials in developing countries. Recognizing this problem, the WBG completed a report on the feasibility, benefits and challenges of implementing AEOI in developing countries, particularly low income countries. In the report, which provided inputs to the Global Forum's AEOI body and to the G20 Development Working Group, the WBG encouraged a flexible approach to implementation, which vested developing countries and non-financial centers with the authority to decide whether to move towards

²⁶ In addition to restricting IFC and MIGA financing for certain transactions through intermediate jurisdictions rated from time to time as partially or non-compliant by the Global Forum, the OFC Policy has also accommodated support to countries from the Bank to take steps required to be compliant with Global Forum standards. Capacity building provided to complement the OFC Policy has been instrumental in countries like Peru in improving de facto practices and de jure rules in relation to tax transparency and the provision of tax information.

implementing AEOI and the speed of adoption. For those countries who have elected to adopt AEOI, the WBG, jointly with the OECD, provides technical support on both the product and receipt of bulk transfers. Pilot efforts are underway in Colombia, Pakistan and Albania.

26. Work strengthening the capacity of tax authorities is complemented by a growing effort in strengthening the capacity of law enforcement officials to identify and sanction illegal tax behavior. This work has recently been initiated due to rising interest on the part of clients to use all available instruments to clamp down on tax evasion. Current efforts are primarily focused on the creation of a toolkit for law enforcement agencies on recognizing and stopping tax evasion schemes in high-risk areas. A strongly connected effort is exploring ways to expand current assessments of anti-money laundering risks to include those related to tax evasion. This engagement will be described in greater detail in subsequent sections of this note.

2.2b Extractives and Natural Resources Integrity²⁷

27. Existing information suggests a strong association between extractive industries and IFFs. Many of the countries with the largest volume of IFFs feature large oil and gas sectors.²⁸ This may be an anomaly caused by particular problems with trade statistic data as well as a reflection on the elevated risks of corruption and international fraud in this arena. A substantial body of literature on extractives has detailed corruption in determining resource management strategies and the assignment of rights to exploitation, and oftentimes, illegal production. Theft, cross-border smuggling, abusive transfer pricing, and manipulation of commodity trading have been studied and documented. Within its overall work in the sector, the WBG helps governments build capacity to design, sign, and manage contracts in extractive industries at the same time that it increases monitoring and oversight of these processes. Through this work, the WBG is building partnerships among private sector firms, governments, and civil society that are essential to changing behaviors, incentives, and outcomes relating to IFFs.

28. The WBG supports effective and transparent contracting in the extractive industries. Upon request, the WBG makes available expert transactional specialists to clients to help design and negotiate fair and equitable contracts in the extractive sector. Technical assistance is funded through the African Sustainable Extractive Industries Facility (ASEI), and serves to both improve the transparency of the contracting process and the quality of the contract.²⁹ WBG support for the greater contractual transparency is also provided through the creation of a global repository of petroleum and mineral contracts. Developed in partnership with the National Resource Governance Institute (NRGI) and the Columbia Center on Sustainable Investment (CCSI), ResourceContracts.org looks to help nations increase the resources available to them as they design their extractive contracts. At the same time, the information sharing allows stakeholders to compare contracts in their own country with those found in other jurisdictions. The WBG's support for the Open Contracting in Extractives Initiative assists over 20 countries in making their

²⁷ For an overview of the current WBG engagements in extractive industries, see The World Bank Group in Extractive Industries: 2015 Annual Review, World Bank, 2016.

²⁸ Countries with large extractive sectors such as Russia, Mexico, Malaysia, Nigeria, Brazil, South Africa and Indonesia are all listed among the top 10 sources of IFFs by GFI.

²⁹ Capacity building support for clients for contract negotiations has also been provided by the Extractive Industries Technical Assistance Facility (EI-TAF). With the closing of EI-TAF in 2015, support for strengthening contract negotiating expertise has been taken over by the Extractives Global Programmatic Multi-Donor Trust Fund.

extractive sector contracts publically accessible in a manner that supports improved contracting and contract oversight. The WBG assistance to improving the corporate governance of National Oil Companies is an additional approach to improving the substance and transparency of contracts in the extractive sector, and also has potentially important positive consequences for the management of contracts. The work that is just starting on determining the beneficial owners of firms active in extractive industries can also be expected to encourage better and more transparent contracting.

29. Assistance in strengthening oversight of contract performance encompasses work on following the money, reviewing tax payments, and monitoring the physical extraction of natural resources. Support for the implementation of the Extractive Industries Transparency Initiative is the core of WBG efforts to enhance financial transparency in the sector and enable governments and non-state parties to “follow the money.” The Extractives teams in the Energy and Extractives GP, Governance GP, and IFC work jointly on this agenda primarily through managing a Multi-Donor Trust Fund, with US\$ 68 million in commitments from 15 donors, and engagements in over 50 countries. This effort has been instrumental in establishing platforms at the country level to compare what companies report paying to the government and what governments report receiving. (See Box 5.) Support for the program will continue under the consolidated Extractives Global Programmatic Support Multi-Donor Trust Fund, which will assist the implementation of EITI, at the same time that it intensifies analysis of the information that is being provided in order to enhance tax administration and contract management.

Box 5: EITI – the Nigerian example

Nigeria was the first African government to implement the EITI, beginning in 2003. Among the first initiatives of the National Stakeholders’ Working Group (NSWG) was to commission a comprehensive audit of the entire oil sector value chain to verify that all payments were correct and settled. The audit revealed US\$9.8 billion in outstanding recoverable revenues from 1999 to 2008. The amount includes an estimated US\$4.7 billion owed by the state-owned Nigerian National Petroleum Corporation (NNPC) for payments of domestic crude oil. In response to the audit, then President Obasanjo pledged to comprehensively address the findings to avoid future failures and opportunities for corruption, and to prosecute any clearly identified cases of wrongdoing. As a result, US\$2.4 billion of the lost revenue has been recovered.

The Nigerian experience also has its cautionary dimension. President Obasanjo’s pledge proved to be difficult to turn into action and high-levels of theft continued to be a prominent feature of the oil sector throughout the life of the government. In addition, it is not clear whether the lost revenue was returned to the budget.

30. Improving clients’ ability to identify and prevent tax evasion in extractive industries is an increasingly important component of the WBG’s contribution to preventing IFFs. Growing demand for dedicated capacity building from revenue authorities in resource-rich countries is prompting efforts to distill guidance and assessment tools that can help address IFF risks. Responding to that demand, the Energy and Extractives Global Practice, working in close coordination with the Governance Global Tax Team, have assisted countries looking to strengthen their mining tax administration. Studies of tax administration in the mining sector in Mali, Burkina Faso, Ghana, Tanzania, and Namibia have provided the basis for assistance in preventing tax evasion, and for a series of workshops for officials in the Ministry of Mines in South Africa,

Tanzania, and Ethiopia. These country experiences also helped build a sourcebook on improving tax administration in mining.³⁰

31. **The WBG is also supporting the use of advanced technologies to monitor the physical extraction of resources.** Technologies, such as smart phones, drones, and satellites can radically enhance the ability of governments and stakeholders to monitor the activity of concessionaries and holders of rights for mineral extraction. The WBG is actively involved in sharing knowledge and making expertise available to countries in order to enable official monitoring of the manner in which firms and individuals are exercising their extractive rights and support rapid detection of transgressions.

32. **Support for effective monitoring is also a dimension of the WBG’s technical assistance to member countries in meeting their commitments in the Kimberly Process and the International Conference of the Great Lakes to take action to stop the smuggling of diamonds and other conflict minerals.** Increasing the capacity of governments in fragile and conflict states to manage their natural resources is both a challenge and a necessity and is a place where the negative impact of IFFs on development is most severe.

2.2c Trade Policies, Economic Regulation, Customs and Border Crossings

33. **In its efforts to enhance trade and competitiveness, the WBG assists clients and stakeholders in the prevention of activities that give rise to IFFs.** Programs of work exist around preventing specific illegal activities (illegal logging, illegal fishing), as well as efforts that encounter illicit practices in a broader range of activities, such as customs and border control.

34. **A substantial portion of the WBG’s efforts in this area is analytical work.** The WBG has undertaken a variety of relevant studies – from analyses on shadow economies, non-tariff trade barriers, and corruption in customs authorities, to studies of piracy, trafficking in wildlife, or illegal logging and fishing. Recent studies of the size of the informal trade in Tunisia,³¹ the role of trading firms in tax evasion,³² and the ability of politically powerful firms to evade taxes³³ have demonstrated the salience of activities relating to IFFs to the overall trade agenda, and the importance of specific types of firms in trade practices. (See Box 6 for an example of how analytic work informs operations.) The WBG has also produced a number of tools and relevant frameworks, including the trade restrictiveness index, the Logistics Performance Index, and the Trade and Transport Corridor Management Toolkit.

35. **The WBG’s approach and efforts to support Good Regulatory Practices provide a strong complementary backing to actions against IFFs.** The term Good Regulatory Practice (GRP) generally refers to the systematic application of tools, institutions and procedures which governments can mobilize to ensure that regulatory outcomes are effective and transparent. There

³⁰ See World Bank, *Transfer Pricing in the African Mining Industry – A Reference Guide for Practitioners*, forthcoming.

³¹ Ayadi, Latfi, N. Banjamin, S. Bensassi, and G. Raballand, “Estimating Informal Trade across Tunisia’s Land Borders, World Bank Policy Research Paper, 6731, Dec 2013.

³² Liu, Xuepeng, H. Shi, and M. Ferrantino, “Tax evasion through trade intermediaries: Evidence from Chinese exporters,” *International Review of Economics and Finance*, (2015), <http://dx.doi.org/10.1016/j.iref.2015.10.022>.

³³ See footnote 18 and 19.

is a growing appreciation, including in international organizations, of the benefits of regulatory quality and of the close connection between regulatory quality, trade, investment, competitiveness and good governance. Regulatory transparency measures, such as Notice and Comment requirements related to the promulgation of new regulations, help expose regulations which may provide excessive discretionary authority and loopholes to regulated entities or their supervisory institutions. At the same time, other systemic measures by governments such as the introduction of Regulatory Impact Assessment (RIA), on-line regulatory registries and IT-enabled mechanisms to issue licenses, are likely to root out many IFF opportunities before they even materialize.

Box 6: Customs and Corruption in Madagascar

In Madagascar, within the framework of the preparation of a PforR on modernization of the public sector, statistical analysis and sectoral studies have been carried out to identify and estimate roughly the level of customs fraud. This work is being complemented by a political economy study of the private sector in order to better understand the current practices that influence civil servants' decisions. The mirror statistics analysis was presented to the DG customs and private sector representatives, and particular brokers/importers were identified. The main findings of the analytical work have been used to inform the PforR components on customs and tax reforms and the decision to use performance contracts in customs.

36. The World Bank's Good Regulatory Practice program—supported financially by DFID and USAID—helps governments enhance the quality of regulatory regimes and their outcomes, and put in place effective, transparent and accountable reform processes that assist in reform prioritization, design, and implementation. The Program is implemented jointly by the Governance Global Practice, the Trade and Competitiveness Global Practice, and DEC's Global Indicators Group. On the basis of knowledge products developed in 2015-2016, the GRP Program is now in the process of implementing country-level pilots in support of transparent and inclusive consultation practices, business feed-back to regulators, and impact assessment systems.

37. An extensive program of support for improved border controls and customs operations addresses a critical arena for preventing illegal trade practices. Over a period of 20 years, the WBG has supported over 120 customs, border, and trade facilitation projects that have dramatically improved the effectiveness of service provision. Through this project experience, the WBG has gained extensive expertise and an improved understanding of the dynamics of corruption in customs operations and the tensions among the objectives of enhanced trade facilitation, border control, and effective customs operations. Innovations, like the use of performance contracts for firms and high-level officials have been introduced in order to properly align the incentives of officials to achieving multiple objectives, often with very constructive results.³⁴

³⁴ See Thomas Cantens, Robert Ireland & Gaël Raballand (2015) Introduction: Borders, Informality, International Trade and Customs, *Journal of Borderlands Studies*, 30:3, 365-380, DOI: 10.1080/08865655.2015.1068207 for a discussion of managing the trade-offs. See also Raballand, Gael; Marteau, Jean-François; Mjekiqi, Edmond; Cantens, Thomas (2009): Could a well-designed customs reforms remove the trade-off between revenue collection and trade facilitation?, *Proceedings of the German Development Economics Conference, Frankfurt a.M. 2009, No. 28*. For a discussion of an actual case example, see Cantens and Raballand, *A New Approach to Customs Reform in Sub-Saharan Africa: The Cameroon Performance Contracts Initiative*, World Bank Research Workshop Impact Evaluation of Trade-Related Policy Interventions: Paving the Way, Dec 2010.

2.2d Anti-Corruption

38. **The WBG provides broad support in the area of anti-corruption to help clients identify risks, detect corruption trends, and design and implement anti-corruption strategies.** Work on establishing approaches to combat corruption is complemented by technical assistance to anti-corruption authorities and to judicial institutions. Support for public sector integrity is enhanced through extensive work on increasing transparency in public financial management and increasing the public availability of information to enable citizens and civil society groups to hold government accountable. While this work does not specifically target corruption related to illicit financial flows, it is an essential element of a holistic response to preventing a source of illicit financing and a factor that helps address illicit activities.

39. **The WBG has an extensive history working on anti-corruption, and has been at the forefront of exploring the relationship between corruption and development and developing the key analytical tools for assessing and diagnosing corruption.** The World Wide Governance Indicators was among the first rigorous efforts to assess corruption in countries across the globe and continues to be widely used and cited. Subsequent methodologies, such as the “value chain” approach that was presented in *The Many Faces of Corruption* book have enabled countries to analyze their exposure to corruption and take remedial action.³⁵ The Bank has extensive experience with the application of these tools and in supporting country-led efforts to establish anti-corruption strategies based on these empirical inputs.

40. **The WBG has supplemented support for anti-corruption strategies with capacity building efforts involving a wide variety of state and non-state institutions.** The Bank has extensive experience assisting in the creation of anti-corruption agencies and helping to develop their procedures and competencies. That support has often featured work on implementing asset-disclosure systems that increase the possibilities for oversight and monitoring of the wealth of public officials and identifying conflicts of interest. Contributions to regional networks of anti-corruption agencies has become increasingly prominent in the WBG’s work program, especially in Latin America. The movement to regional networks reflects the value such bodies can have for exchange of good practices and in developing relationships that are essential in dealing with cross-border issues.

41. **WBG assistance to strengthen justice and rule of law also features support to regional networks of practitioners and policy makers.** JUSTPAL, the Justice Sector Peer Assisted Learning Network, initially established in 2011 for ECA countries and now a global forum for peer-based support and learning for justice sector performance improvements, is a prime example of a network established to share expertise and experience in improving justice sector entities’ performance (e.g. courts, prosecution, anti-corruption agencies and ministries of justice) and to assist countries in designing and implementing justice reforms.³⁶ Two key demand-based products from JUSTPAL have been: (i) justice performance indicators (Justice At A Glance or JAAG) for all ECA countries; and (ii) an analytic product (Justice Sector Public Expenditure and Institutional

³⁵ See Campos, J. Edgardo; Pradhan, Sanjay. 2007. *The Many Faces of Corruption: Tracking Vulnerabilities at the Sector Level*, Washington, DC. World Bank.

³⁶ For a discussion of JUSTPAL, see World Bank, *Innovative Governance and Anti-Corruption Initiatives: A Selective Survey of Recent World Bank Activity*, World Bank, 2014.

Review or JSPEIR), completed for Bulgaria, Croatia and Serbia and being initiated in 2016 for Azerbaijan, Kazakhstan, Moldova and Ukraine. JUSTPAL complements efforts at the national and regional (e.g. EU) level that have often had a particular focus on corruption and justice. The long-standing justice engagement in Croatia significantly strengthened the impact of justice sector entities engaged in combatting corruption and assisted in Croatia's fulfilment of key criteria for its accession to the European Union. A similar exercise was conducted for Bulgaria before and after its 2007 accession to the EU. In addition, the Bank's ongoing support since 2008 for Serbia's justice sector reforms has been supported by multilateral and bilateral partners. Recently initiated justice support engagements in Ukraine and Moldova will build on lessons learned from these successes.³⁷

42. **The International Corruption Hunter's Alliance, established by the WBG, brings together law enforcement officials across the globe to enhance collaboration and share expertise.** ICHA was launched in 2010 with the support of the Governments of Australia, Denmark and Norway. (See Box 7.) The overall objectives of ICHA are to strengthen the performance management of law enforcement authorities; facilitate sharing practical and cutting-edge solutions to address corruption, and encourage the flow of information among law enforcement bodies. The WBG also provides capacity building support to law enforcement officials related specifically to mutual legal assistance and technical assistance in undertaking asset recovery actions within the context of its support on anti-money laundering and asset recovery.

Box 7: International Corruption Hunters Alliance

Advancing IFF solutions through international cooperation on anti-corruption

The World Bank's International Corruption Hunters' Alliance (ICHA) is a global network of heads and senior officials of investigative and prosecutorial authorities and anti-corruption agencies with an enforcement mandate. Since 2010 members of the Alliance have met on a biennial basis at the World Bank headquarters to learn about emerging tools, policies and practices in fighting corruption, and to establish relationships that are so vital in cross-border cooperation. The link between corruption and illicit financial flows was the focus of a plenary session at the 2014 meeting of the Alliance.

43. **Engagements on anti-corruption are mirrored by engagements related to building public integrity.** The WBG has a very active portfolio of work on enhancing public financial management transparency and oversight. The portfolio includes engagements on increasing the flow of information relating to public spending, such as public procurement, as well as strengthening the capacity of audit agencies, parliaments, and civil society to use that information to hold government officials to account. The WBG's participation in the Global Initiative for Fiscal Transparency reflects an appreciation that efforts to enhance fiscal transparency may be best accomplished in partnership with other organizations and using a global platform.

44. **At an operational level, the World Bank Group is leveraging its investigative, fiduciary, and preventive work to inform the design and supervision of high integrity risk operations and Country Partnership Frameworks.** The aim is to reduce these operations' vulnerability to corruption and to use them as vehicles for strengthening national integrity systems. Investigation reports are referred to national law enforcement authorities in order to provide evidence to assist their follow-on investigations. The Bank is also working with clients to reduce

³⁷ See World Bank, Croatia: A Chronicle of Selected Justice Reforms: Achievements, Challenges, and the Road Ahead, World Bank, 2014.

the vulnerabilities identified in investigations by the Integrity Vice Presidency (INT)—including those related to transnational corruption and international cartels. Complementary work to strengthen mechanisms for citizen engagement and beneficiary feedback in projects supported by the WB has greatly enhanced the flow of information at the operational level and strengthened the ability to identify corrupt practices. Further work is needed to better understand how international development projects, such as those financed by the WBG, become vulnerable to tax evasion, organized crime, and other criminal conduct resulting in illicit flows.

2.3 Stopping Illicit Financial Flows

Anti-Money Laundering and Asset Recovery

45. **The WBG works with developing countries to develop and use “follow the money” tools to prevent, detect, and combat IFFs and the underlying activities such as corruption, organized crime, environmental crime, and tax evasion.** In addition, the Bank advocates for financial centers to take action in their own countries against the laundering of the proceeds of corruption and monitors their progress against international commitments. To this end, the WBG Financial Market Integrity team conducts evaluations of anti-money laundering (AML) regimes against the international standard, provides capacity building to policy makers and practitioners across the range of institutions and expertise relevant to AML (legal drafters, supervisors, law enforcement, criminal justice, international cooperation, and use of financial intelligence), informs policy makers and practitioners with cutting edge knowledge products, and uses its convening power to push for improvements at country and international levels.

46. **Closely linked to its “follow the money” work is WBG assistance to countries in tracing, freezing, and recovering stolen assets that represent the proceeds of corruption delivered through the Stolen Asset Recovery Initiative (StAR), a joint initiative of the World Bank Group and the United Nations Office on Drugs and Crime.** StAR works with developing countries to prevent the laundering of the proceeds of corruption and to facilitate more systematic and timely return of stolen assets.³⁸ In support of this agenda, StAR helps requesting countries build their capacity to trace stolen assets through the financial system and to request mutual legal assistance from financial centers to freeze, confiscate and return the stolen assets. This includes training practitioners on use of “follow the money” tools, conducting cases and requesting international cooperation. In addition, the StAR mandate goes further by allowing support to countries with actual cases. StAR’s assistance in these cases focuses on providing practical advice and management of asset recovery cases, as well as acting as a facilitator between the various jurisdictions involved in the asset recovery effort. These programs were confirmed and further operationalized following the *World Development Report 2011*.³⁹ See Box 8 for examples of the range of assistance StAR has provided.

³⁸ StAR contribution to the recovery of stolen assets was recognized in the Financing for Development Communique. Target 25 “encourage(s) the international community to develop good practices on asset return. We support the Stolen Asset Recovery Initiative of the United Nations and the World Bank and other international initiatives that support the recovery of stolen assets.”

³⁹ See World Bank, “Operationalizing the 2011 World Development Report: Conflict, Security and Development” (Washington, DC: World Bank: 2011); see also World Bank, “Legal Note on Bank Involvement in the Criminal Justice Sector,” Senior Vice President and General Counsel (Washington, DC: World Bank, 2012); and World Bank, “Staff Guidance Note: World Bank Support for Criminal Justice Activities” (Legal Vice Presidency, February 2012).

Box 8: Examples of assistance StAR has provided to countries

- **Multi-faceted engagement: Tanzania**, where an engagement developed into assistance across a number of areas. In 2014, StAR assisted the development of a strategic plan by an asset recovery institution to support the successful investigation and prosecution of asset recovery cases. A StAR-funded mentor began her work advising another asset recovery institution in the implementation of the strategic plan developed with StAR assistance in 2013. Additional ad-hoc assistance was given in advising on cases, and in reviewing a draft law on non-conviction based forfeiture. StAR will be providing capacity building of judicial officers on asset recovery matters in 2015, to support Tanzania's asset recovery efforts throughout the process.
- **Use of innovative legal tools: El Salvador**, where StAR provided capacity-building training to enable a new law on Non-Conviction Based Asset Forfeiture (NCB) to be used. The authorities wanted to develop this tool as an additional required element for asset recovery. Training was delivered by StAR's Vienna-based UNODC personnel, illustrating the seamless cooperation between it and World Bank staff in the delivery of assistance on the ground.
- **Engagement in fragile and conflict-affected states.** StAR assisted **Somalia** in the development of an asset recovery strategy, including policy considerations on the management of recovered assets. StAR has also provided guidance to Somalia on good practices in engaging private sector entities in asset recovery actions. In **South Sudan**, StAR provided case-related technical assistance 2011 - 2013, supporting the Ministry of Finance with an assessment of liabilities in the wake of a procurement scandal, as well as support to the South Sudanese Anti-Corruption Commission with the draft anti-corruption bill and the implementation of asset disclosure legislation. Activities were suspended in 2013 due to the civil conflict. The South Sudanese authorities contacted StAR again in 2014, requesting case-related assistance to conduct a similar assessment of liabilities with a much broader scope. In October, StAR undertook a scoping mission and provided proposals for next steps, which were awaiting a response from the authorities in Juba (prior to the outbreak of renewed hostilities in the country in 2015).
- **Addressing new requirements arising from training.** In **Moldova** StAR provided capacity building and technical assistance, to assist the authorities following the passing of new legislation on illicit enrichment. In addition, StAR is also working with the authorities to improve their asset declaration systems and processes, and as part of a broader World Bank supervision team.
- **Facilitating and coordinating key international gatherings – The Ukraine Forum on Asset Recovery (UFAR) and the Arab Forum on Asset Recovery (AFAR)** both of which were unique in bringing together requesting countries, financial centers, international organizations and others, in single location at the same time to address specific issues. UFAR and AFAR were arranged by StAR at the request of key international players, and demonstrated StAR's unique capability, contacts and expertise to facilitate such an undertaking. In **Tanzania**, StAR carried out a multi-faceted engagement that included developing strategic plans for asset recovery institutions, capacity building training, and providing a mentor for the Asset Forfeiture and Recovery Section of the Directorate of Public Prosecutions.

47. **Of particular relevance in the context of IFFs is the WBG's National Risk Assessment tool developed to assist countries in identifying and responding to risks relating to money laundering (ML).** The National Risk Assessment Tool supports countries with analyzing threats, vulnerabilities and risks relating to criminal flows – domestically and cross border. (See Box 9). The tool focuses on all offenses that generate proceeds, including corruption, tax evasion, organized crime, and environmental crime. This fact-based analysis provides a solid basis for countries to deepen their understanding of the extent of their exposure to many of the activities that give rise to illicit financial flows, and to plan ways to mitigate those risks. The process has been undertaken in over 30 countries since 2011, and has proven to be instrumental in defining priorities and establishing working relationships with agencies that might otherwise not interact.

Box 9: Money laundering (ML) National Risk Assessment (NRA)

The World Bank Group’s National Risk Assessment Tool is an advisory package that supports countries with identifying, assessing and understanding their ML risks – a necessary step that enables countries to target scarce resources to areas where they will have the biggest impact.

The Tool comprises several interrelated modules that represent features connected to ML threats and vulnerabilities. “Threats” refer to the various crimes that generate proceeds of crime in a country (e.g. corruption, tax crimes, organized crime). “Vulnerabilities” consider the weaknesses or gaps in a country’s defenses against ML.

The Tool uses a systematic and organized process that is led and owned by the country, with the broad participation of public and private sector stakeholders. Both qualitative and quantitative data are relied upon for the assessment.

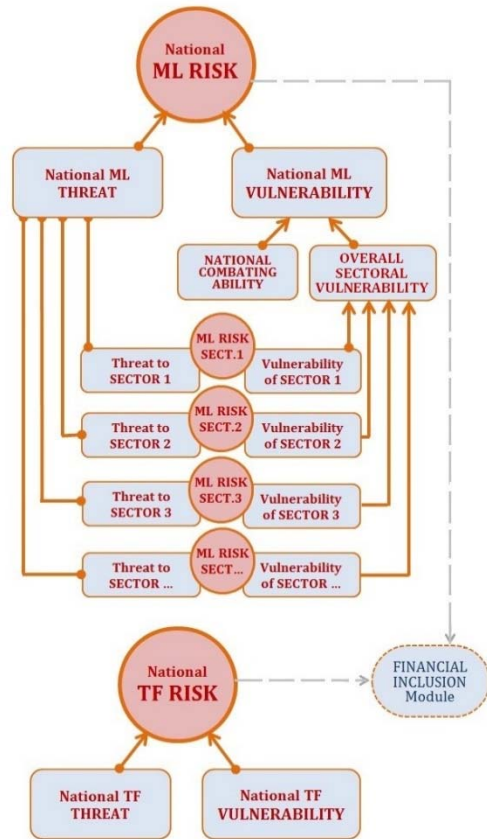
The Tool was developed around the standards established by the Financial Action Task Force (FATF) to protect the integrity of global financial markets.

Example: NRA in Peru

The Detailed Risk Assessment being undertaken in Peru is an example of how the NRA can be adjusted to focus on specific sectors of concern. The main objective of the Peru effort is to assist the Peruvian authorities in carrying out detailed risk assessments in the financial, mining, and fisheries sectors, with a view to complement their comprehensive ongoing National Risk Assessment (NRA).

Building upon the methodology that the WBG designed for countries to assess their money laundering risks and threats, and to determine priorities, the sectoral assessment fills in gaps that the more general NRA may not be able to identify and leads to more sector oriented action plans to combat and prevent ML. It can also serve the purpose of determining whether an AML approach is best suited for these issues or whether a broader, more comprehensive public policy is required, particularly from the illicit financial flows perspective.

The findings of these detailed assessments should assist the Peruvian authorities in prioritizing efforts to combat illegal activities (including but not restricted to AML efforts) and allocating limited resources effectively in order to mitigate identified risks. Having a detailed analytical sectoral assessment, as well as an action plan that is based upon the findings of this sectoral assessment, supports more informed policy decisions and effective regulatory designs.



48. **Support to developing countries in addressing risks to financial integrity and recovery of stolen assets is matched by strong engagement at the global level.** For their part, developed economies have signed off on key international standards as a means to level the global playing field on transparency, AML systems and international cooperation (e.g., United Nations Convention against Corruption, UNTOC, Global Forum, the Financial Action Task Force and G20). The WBG is actively engaged in this process through its global engagement work—advocating changes to the respective standards, developing knowledge to influence policies, assessing countries against their international commitments, and using the WBG’s convening power to support international cooperation. The WBG and StAR have contributed to important changes in standards on beneficial ownership, asset disclosure, asset tracing, international

cooperation, and asset recovery in forums such as the Global Forum, G20, G8, FATF, UNCAC, and the Asia-Pacific Economic Cooperation.⁴⁰

49. **The World Bank’s engagement with the private sector, and notably the financial sector, has been more indirect, and relied essentially on working through the public sector.** In this context, the World Bank has actively participated in regular meetings between the FATF and the private sector, or advocated for a dedicated dialogue between the G20 Anti-Corruption Working Group and the financial sector. Such a dialogue was initiated in October 2015 during the Experts Meeting on Corruption of the FATF and G20 ACWG.⁴¹ In addition, the WBG, through its participation in the annual meeting of the Wolfsberg Group,⁴² actively engages with the international banking community to find ways to build effective partnerships with financial institutions in combating illicit financial flows.

50. **The WBG’s work on beneficial ownership demonstrates the full range of engagements on stopping illicit flows, as well as the importance of WBG contribution.** The WBG has been at the forefront of the international policy discussion on beneficial ownership beginning with the 2011 StAR publication “The Puppet Masters: How the Corrupt Use Legal Structures and What to Do About it.” The study was an important reference point in the revision of international standards on AML by the FATF in 2012 and the adoption of the G20 High Level Principles on Beneficial Ownership Transparency in 2014. More recently, StAR has been working with the members of the Anti-Corruption Working Group of the G20 to draw up country guides to beneficial ownership to facilitate the understanding by foreign jurisdictions of the country’s laws and regulations on legal entities and arrangements, and provide practical guidance on how to identify the beneficial owner of a particular corporate vehicle incorporated or established under the laws of that country. (See Box 10). To date, fourteen country guides have been finalized.

3. Building on foundations – a proposed way forward

3.1 Seizing the momentum

51. **WBG experience in addressing IFFs is a strong foundation on which to base future efforts.** Past and on-going work provides an informed perspective on what is needed in order to catalyze change and the challenges that exist to reduce IFFs and their impact on development. The prominence of illicit financial flows in public discourse and current developmental dialogues open up new opportunities for action at both country and international levels and it is critical for us to make use of these new possibilities to reduce the flow of IFFs.

⁴⁰ WBG input relating to the issue of beneficial ownership has been particularly consequential. Since the publication of its study on beneficial ownership “The Puppet Masters” in 2011, the StAR initiative has been at the forefront of the international policy discussion on beneficial ownership. The study was a key reference in the revision of the international standards on Anti-Money Laundering (AML) by the Financial Action Task Force in 2012, notably recommendation 24 on the transparency of legal entities. StAR was a key discussion partner in the drawing up of the G8 principles on beneficial ownership, endorsed in June 2013, and the G20 High-Level Principles on beneficial ownership, agreed in November 2014.

⁴¹ <http://www.fatf-gafi.org/publications/documents/experts> meeting October 2015.html

⁴² The Wolfsberg Group is an association of thirteen global banks which aims to develop frameworks and guidance for the management of financial crime risks, particularly with respect to Know Your Customer, Anti-Money Laundering and Counter Terrorist Financing policies.

Box 10: Revealing ownership—the challenge of implementing constructive beneficial ownership rules

Determining the true identity of the owners of companies is increasingly central to the effort to stop money laundering, recover stolen assets, and prevent international fraud and corruption. In the vast majority of cases involving high value financial crime, criminals or their accomplices will employ a legal entity (company or foundation) or arrangement (trust) to conceal their interest in the illegally acquired asset. Thus, it is important that countries' laws provide for the transparency of the so-called beneficial owners of those entities and arrangements if they wish to fight crime. Unpacking the ownership of firms is also central to efforts to know your client in areas such as tax administration, procurement, and anti-corruption.

Determining true ownership is often neither simple nor easy, especially for agencies with little experience in such efforts and with limited information sources. The WBG is increasingly working with countries in this effort. A large component of our assistance is the technical support offered to countries on defining and implementing rules on beneficial ownership within the context of help in anti-money laundering and asset recovery. This is especially important in smaller international financial centers that serve a large non-resident client base. In FY 15, StAR piloted TA to one such small international financial center on the transparency of the International Business Companies incorporated under their laws and administered by trust and company service providers operating in that jurisdiction. The TA provided both a diagnostic on the current state of play and practical recommendations for improving the transparency of the regime for establishments of IBCs, and could serve as a model for support to other jurisdictions facing problems identifying beneficial owners of their corporate vehicles. Additional work on beneficial ownership is being done as part of our efforts on tax evasion, governance in Extractives Industries and in procurement.

52. **The WBG's role as an honest broker, its deep engagement on development policy and experience in reform implementation at the country level suggests that we can play a unique role in advancing IFF work.** Our convening power helps to forge the coalitions of developed and developing countries, and state and non-state actors, that are essential to tackling IFFs. Our expertise and experience in analytical work related to IFFs and the activities that generate illegal revenues places us at the forefront of measuring IFFs at the country level and using the analyses to identify targeted actions. Our portfolio of interventions in areas from trade policies to financial asset declarations gives us insight into how government, business, and the financial sector interact and helps us to provide platforms to operationalize change. Our role in helping to shape global agendas at the same time that we support the implementation of country specific reforms enables us to integrate global efforts into country activities and to inform the design and implementation of global standards with information about realities on the ground.⁴³ Our various interventions, from supporting the implementation of EITI to helping countries recover assets through the StAR initiative have demonstrated our operational competencies and our ability to produce results. They have made us a trusted partner of governments, the private sector, and civil society.

53. **At the same time, the WBG can ensure strong linkages and draw out synergies in the areas of work carried out to date.** Efforts at prevention, detection, and sanctioning of illicit activities and illicit financial flows have remained largely in silos. Engagements related specifically to stopping financial flows have relied heavily on the action of regulators and law enforcement officials in developing countries, often without the benefit of data from monitoring and checking on the cross-border movement of goods and financial assets. Work on improving oversight and transparency in the management of natural resources or public finances has not capitalized on information from efforts to reduce money laundering or facts uncovered during the

⁴³ A recent example of the WBGs work on establishing global partnerships is the Global Partnership on Wildlife Conservation and Crime Prevention for Sustainable Development – a US\$91 million, five-year program to support country specific efforts and international collaboration to address illegal wildlife practices and trade.

course of asset recovery cases. Without a way to measure changes in the volume and impact of IFFs, monitoring efforts have often emphasized inputs and commitments to act instead of outcomes. By joining up different WBG efforts and drawing more on partnerships, the WBG can better help countries establish prioritized and sequenced strategies to reduce IFFs.

54. **Going forward, WBG efforts on IFFs will seek to extend the range and depth of our IFF engagements; draw the linkages across the different work streams; and better leverage country, regional, and international partnerships.** Specific activities will be determined by the demands for our support from our clients and partners, and the availability of resources. Until now, requests for support for integrated efforts to address IFFs have been very limited and it remains to be seen the extent to which the enhanced awareness of the phenomenon will trigger client demand. However, the WBG can do more to demonstrate that a more integrated approach can lead to greater impact.

55. **The WBG will continue to provide support to clients in three principal areas: measuring IFFs; preventing the activities that give rise of IFFs; and stopping the flow of illicit funds and returning stolen assets.** This work will continue to feature efforts at both country and international levels, and include analytical work (e.g., measuring flows or assessing governance in the Extractive Sector), lending operations (e.g., improving tax administration and customs), and RASs (e.g., anti-money laundering). A number of these activities are supported by Trust Funds that have been created specifically to enable this work to take place. Other activities will need additional sources of funding.

3.2 An Action Plan for Going Forward

56. **We will continue to develop our approach as we learn from our experiences.** Going forward over the medium-term, we will focus on five strategic efforts:

- improve tools to monitor and measure IFFs
- develop greater integration across interventions at the country level
- explore the lessons from StAR and their relevance for recovering other IFFs
- build capacity in critical areas for reducing IFFs
- strengthen global coalitions to reduce IFFs

Improve Tools to Monitor and Measure IFFs

57. **First, the WBG will improve tools to monitor and measure IFFs.** Analytical tools that enable IFFs to be identified and measured are essential to developing well-targeted interventions and evaluating impact. As noted above, the WBG, along with individual countries and development partners, has already established a range of analytical tools to measure different dimensions of the IFF issue. The WBG will lead an effort to further refine the existing instruments to create and field methodologies to assess, diagnose, and monitor IFFs at the country level.

58. **The WBG will develop an IFF Rapid Assessment Tool to help countries assess their exposure to IFF outflows and inflows.** The rapid assessment tool will draw upon and combine existing data sources. Outflows are expected to be assessed primarily by combining existing assessments in the area of tax administration, governance, and money laundering. Inflow

assessments will initially rely upon a range of sources regarding capital flows and money laundering as well as information on the transparency of financial systems. The Rapid Assessment Tool will enable countries to identify their level of risk and can be used to inform subsequent discussions of where an IFF perspective to organize work might be most useful. In the medium term, this tool will be enhanced to undertake a more detailed analysis of the nature of the IFF risks faced by a country, including the nature of the IFF challenge. This enhanced tool would be expanded to address tax evasion more comprehensively. Diagnostic tools developed by DEC, the Global Tax Group, the Governance Group, and Trade and Competitiveness will be drawn upon.

59. **The measurement of IFFs relates to the nature of the origins of the flows and needs to be undertaken at the country level.** The WBG and others have developed a variety of approaches to assessing different dimensions of IFFs. Where there is demand, the WBG will assist in strengthening the methodologies for measuring specific flows, in partnership with countries, development partners, and research institutions to establish a measurement tool.⁴⁴ Based on past experience, these efforts are costly and require significant investments.

Develop greater integration across interventions at the country level

60. **Second, the WBG will increase linkages across related engagements at a country level.** Current efforts frequently exist in isolation from each other due to the absence of a common IFF perspective. For example, efforts to increase the transparency of revenues derived from extractives industries may happen in parallel with efforts to strengthen auditing in the same country, without the coordination which could increase impact by linking the two interventions. The WBG will take concrete steps to enhance the integration of activities related to IFFs. As a first step, the WBG will make use of the Rapid Assessment Tool to inform Systematic Country Diagnostics and subsequent Country Partnership Frameworks. Country IFF risk assessments will be supplemented by standard information already captured in the SCD process but which has not been linked up previously. Where indicated, the country team, in partnership with the client, may also choose to undertake a more extensive analysis of its exposure to IFFs as part of the SCD process, in order to obtain a more detailed, and action-oriented profile of IFF risks and their potential developmental impact.

61. **The WBG will pro-actively take steps to increase information exchanges across complementary engagements relating to IFFs.** At the request of the client, the World Bank will assist in developing an integrated and sequenced strategy for reducing IFFs, although we anticipate that such requests will come from a small number of countries. See Box 11 for an example of what an integrated country-level IFF approach might resemble. In addition to a range of activities designed to strengthen policies and change public and private behaviors, a country-level IFF strategy may include creating an IFF baseline using the IFF measurement tools and developing capacity to undertake subsequent monitoring of change. Responses to requests for IFF strategies would likely take the form of ASAs or RASs.

⁴⁴ The creation of modified tools will include careful consideration of the potential for new technologies to facilitate identification and tracking of illicit activities, be it satellite monitoring of illegal fishing or more terrestrial sensors for spotting oil “bunkering.”

Box 11: WBG Work in Tunisia – a program of complementary activities

Strategic partnerships between the WBG and the Tunisian Ministry of Finance and the Tunisian Institute of Statistics assembled a unique database comprising tax, social security, and customs transactions records of 655 firms owned by the Ben Ali family. Analysis of the data set revealed the extent of the family's holdings and the manner in which they used their public power for private gain. Illegitimate wealth was obtained through influencing the implementation of investment regulations, privatizing public assets into private hands at severely discounted prices, and tax evasion. The analysis estimates that the family evaded at least US\$1.2 billion worth of import taxes between 2002 and 2009 by under-invoicing of prices alone.

The analysis has also led to a broad program of WBG support to Tunisia for trade reforms that would reduce the cost of formal trade, including with neighboring countries, and reduce the incentives for informal trade. The main vehicle for this work is the Third Export Development Project (US\$50 million, effective since September 2015), with a focus on reducing delays in goods processing; increasing customs efficiency, transparency and governance by improving the risk management system; reshaping the control policy; and reducing human intervention in customs activities. With the support of the WBG, the Government of Tunisia has moved to simplify and reduce import tariffs and is exploring ways to increase transparency regarding the enforcement of non-tariff trade regulations. The Bank has also been discussing with Tunisia Customs setting up a regional data exchange with Maghreb countries to increase transparency over trade regulations and other important border information.

The WBG and StAR assisted Tunisia in designing a comprehensive asset recovery strategy, establishing open channels of communication and information exchange with counterparts in Belgium, Canada, France, Italy, Spain, Switzerland, and USA, which ultimately led to the recovery of assets worth US\$50 million, the acceptance by France and Switzerland of mutual legal assistance requests sent by Tunisian investigative judges, and the identification of bank accounts and corporate vehicles used to launder bribes paid to officials in Panama and the British Virgin Islands. An advisor was posted with the Tunisian Committee on the recovery of stolen assets in June 2012 for six months. In June 2012, a joint StAR-European Union meeting on the Tunisian Asset Recovery case was held to facilitate consultation and exchange of information between Tunisian authorities and the Egmont Group, Interpol, Eurojust, StAR and Law Enforcement Agencies of France, Switzerland, Italy, Spain and Canada.

The WBG is also financing an assessment of the impact and effectiveness of the anti-money laundering regime, conducted in the context of the FSAP and Tunisia's membership in the MENA Financial Action Task Force.

Explore the lessons from StAR and their relevance for recovering other IFFs

62. **Third, the WBG will seek to draw lessons from StAR beyond the proceeds of corruption.** Currently, the WBG engagements on the recovery of IFFs is limited to recovery of the proceeds of corruption—the mandate of StAR. StAR experience may provide insights in the recovery of assets associated with other aspects of IFFs, including tax evasion and trade fraud. Decisions regarding the effective scope of StAR will be informed by requests from international and bilateral partners, and the creation of financing arrangements that support a broader mandate.

Enhance its efforts to build the capacity of clients to reduce IFFs

63. **Fourth, the WBG will enhance its efforts to build the capacity of clients to reduce IFFs.** We will initially focus on two critical areas: (i) detecting and preventing tax evasion in high-risk sectors, and (ii) determining beneficial ownership of firms. These two areas were selected due to their importance for the overall effort to reduce IFFs and current opportunities for making progress based upon the momentum for reform.

64. **Strengthening work on detecting and preventing tax evasion, especially in high-risk sectors such as extractive industries can potentially enable clients to reduce IFFs in the short-term.** Client demand for assistance in improving tax administration has expanded rapidly, in part due to the fall of commodity prices. An important dimension of this work is reducing tax evasion, especially in industries such as extractives, where such practices are especially common. The WBG has already begun to respond to this demand by working with tax authorities and law enforcement officials on identifying illegal transfer pricing and will expand that effort in response to demand. Work may include training, the creation of new procedures and processes to enhance oversight and internal controls, and the strengthening of rules to increase transparency around the granting of tax concessions, and the content of those agreements.

65. **Increasing the capacity of clients to determine the true ownership of firms is important for preventing and detecting corrupt behavior and the recovery of stolen assets.** Rules requiring the provision of detailed information on beneficial ownership are rapidly proliferating. Such rules feature in the FATF requirements as well as in the Global Forum, and have recently been established in the EITI context. Starting in 2017, the WB will begin to require such information for winning bidders in higher-value procurements undertaken in projects supported by the World Bank. These requirements are unlikely to be successfully without a dedicated effort to build the capacity of public and private institutions to determine, record, and report on ownership information. The value of such information is also likely to be diminished without the creation of standard electronic formats for data. The WBG already provides assistance to clients on generating beneficial ownership information and will expand that assistance in line with new demands and requirements.

Strengthen global coalitions to reduce IFFs.

66. **Finally, the WBG will contribute to global engagements both by drawing on experience to inform global standards and by helping countries to implement their international commitments on IFFs.** WBG efforts to inform international standards, to participate in the review mechanisms of these standard setting bodies, and to provide support to the evaluations and capacity building of individual countries is critical to this agenda. As the WBG collects more information on the composition and destination of IFFs in the context of country work (e.g., the NRA Tool), the WBG will also be able to mobilize this additional knowledge to engage these bodies and relevant jurisdictions to advocate for improvements that may emerge at the global and country levels.

67. **The WBG can also serve a critical coordinating role.** Given the cross-border nature of IFFs, international cooperation is essential. In a world where money can be transferred to a foreign account at the click of a button, formal mutual legal assistance is slow and cumbersome, ultimately thwarting prosecutions and recovery of assets. Law enforcement practitioners do not always trust their foreign counterparts and refuse to share information and intelligence. The 2011 StAR publication on “Barriers to Asset Recovery” explored the sources of these barriers in international cooperation—in laws, institutions and operationally—and is a starting point for future knowledge work that could focus more directly on international cooperation. Similarly, the role that StAR has played as ‘honest broker’ between requesting and requested countries provides an entry point for the WBG to add value. Following the model of the WBG’s work on transparency and beneficial

ownership, the WBG can use our knowledge, convening power and advisory services to add value on this issue—at the global level and for the benefit of all our stakeholders.

68. **Building on and strengthening partnerships is fundamental to a sustained and successful effort to address IFFs and the underlying activities.** No single institution or country has the resources and ability to address the scale, scope, and diversity of IFFs. A variety of collaborative efforts that are actively engaging with IFFs already exist. Engagements led by FATF and the Global Forum, are very different from those relating to EITI and the Kimberly Process but share the common features of bringing together state and non-state parties to change rules, behaviors, and incentives. These dynamic partnerships are likely to be increasingly central to the IFF effort and require strengthening as well as deepening. Organizations such as the European Union, African Development Bank, Asian Development Bank or the Common Market for Eastern and Southern Africa, are essential partners in supporting cross-border collaboration in confronting IFFs. At the international level, it is vital to continue engaging with a broad range of partners (e.g., UN family, OECD, IMF, FATF, Global Forum on Taxation.) to support cross-border collaboration, monitor the implementation of commitments, and create an international architecture that is most conducive to equitable and transparent economic activity. Within the overall context of implementing the global commitment to reduce IFFs in the Sustainable Development Goals, work is required at the global level to support policies, standards, and collaborations that enhance the effort to reduce IFFs. In undertaking actions in the five areas discussed above, the WBG further strengthens its ability to support global efforts to reduce IFFs, drawing upon its in-depth country work and its strong network of global partnerships.