The Financial Secrecy Index and Corruption

The Financial Secrecy Index draws attention to the provision of international financial secrecy. This has enormous significance for questions of corruption, and in turn introduces a "second wave" in global understandings and solutions to that problem.

A Brief History of Corruption

Incredibly, until the mid 1990s corruption did not feature in the practical discussions of international development. Despite having been a problem for at least half a century – as dictators siphoned their nations' wealth into secret offshore bank accounts, petty bribe-taking grew, and official dishonesty destabilised the governments of many developing nations – corruption just wasn't on the agenda.

This changed with the launch of Berlin-based Transparency International in 1993. Transparency International drew attention to the endemic problem of corruption, launching the seminal "Corruptions Perception Index" [link] in 1995. The World Bank – which had previously all but banished the "c" word from its policy documents – accepted in a landmark 1996 speech that the Bank needed to deal with "the cancer of corruption." In 1999, the OECD's Anti-Bribery Convention entered into force, and in 2003 the UN enacted its Convention against Corruption.

Corruption is now firmly on the agenda and our understandings of how it impacts on development processes is evolving. Corruption has famously been described as *something that happens in other countries*, and to a very large degree the focus of the anti-corruption debate until recently has been on activities happening within the *public sector*: something undertaken by greedy dictators and rotten government officials in the poorer countries. As a consequence, 'corruption' has become almost a byword for bribe-taking.

But the shocking truth is that high-end bribery makes up just a tiny proportion of global illicit finance. Washington-based Global Financial Integrity (GFI) has estimated that the cross-border component of these crimes is the smallest part of "dirty money", at about 3 per cent of the total.

We need a "second wave" in understanding corruption which relocates it as part of a much bigger problem. The Financial Secrecy Index (FSI) is a part of that second wave.

The trillion dollar vanishing act: introducing Illicit Financial Flows

To put corruption into proper perspective, we need to recognise the existence of illicit financial flows. These are defined by GFI as: *"Money that is illegally earned, transferred, or utilised. If it breaks laws in its origin, movement, or use it merits the label".*

Illicit flows are a massive problem. An estimated $1-1.6 *trillion* of illicit funds passes across international borders each year. Recent estimates put the figure for such illicit finance leaving developing countries at $800-$1.06 trillion per annum, which is up to 10 times what developed nations give out in aid.

Illicit finance is a more useful term than capital flight. The latter has become bound-up with established perceptions of corruption, focused on resource-theft and public sector bribery. Illicit finance, by contrast, covers all of the world's dirty money, whoever happens to be handling it and whatever they are handling it for.

In contrast to the relatively small scale of illicit flows originating from bribery, GFI identifies that 30-35 per cent of illicit funds flowing out of the developing world are due to the activities of organised crime. Even more shockingly, they estimate that 60-65 per cent of illicit flows out of developing nations are due to commercially-evaded taxes, driven primarily by falsifying import and export prices. Such tax losses are especially painful for developing nations, since they force states to shift the tax burden onto the poorest who can least afford to pay, ensuring that governments lack the sustainable tax revenues required to invest and develop out of poverty. In many cases this lack of sustainable tax revenues ensures a continued dependence upon the dead-end of foreign aid.

It is the illicit financial flows of the order identified by the World Bank which keep the poorest people on Earth poor. The world needs to catch up, and fast. Fortunately this is quite possible: high-end bribery, crime and abusive tax practices are all joined by a common thread.

The Secrecy Suppliers

The FSI lists and ranks the secrecy jurisdictions which provide financial and legal secrecy. These are the jurisdictions that, with the help of a 'pinstripe infrastructure' of lawyers, bankers, accountants and financial advisers, sell secrecy to those able to afford it.

These jurisdictions are the enablers of illicit financial flows. It is common knowledge that corrupt dictators like former Indonesian President Suharto who expropriate their nations' wealth use secrecy jurisdictions to launder and deposit their stolen assets. The Suharto family reportedly held bank accounts in the Bahamas, British Virgin Islands, Cayman Islands, Cook Islands, Curaçao, Gibraltar, Hong Kong, Panama, Vanuatu and West Samoa. Yet the *very same* jurisdictions facilitate and aid organised crime by providing the financial secrecy which allows money to be laundered and the proceeds of crime to be so lucrative as a result. And the same jurisdictions are used by multinational corporations to create paper transactions and elaborate accounting structures so as to evade legally-due taxes.

It is no accident that these illicit financial flows are attracted to secrecy jurisdictions. Secrecy is what illicit finance thrives off. Secrecy jurisdictions are *crimonogenic environments*: the secrecy they enact means that financial flows cannot be properly traced and accounted for. Behind the secrecy veil, clean and dirty money mingles freely, and one can no longer tell the good from the bad. Such places don't just attract crime, they make it possible.

This has another, very important consequence. The limitation of focusing too narrowly on public sector corruption – bribe-taking and asset-theft in particular – is that the focus of attention shifts away from the *enablers* of corruption. The Financial Secrecy Index purposefully sets out to complement Transparency International's focus on bribery by identifying those who supply an enabling environment for corrupt practices.

The brutal Nigerian dictator Sani Abacha raked billions of dollars of Nigeria's oil wealth into his personal accounts before he died. But *where* were those accounts? *Who* helped him move his money out of Nigeria and into new accounts? *Which* jurisdictions did the money pass through, and eventually settle in? Abacha represented the demand side of corruption, and London, Zurich and other centres of international financial secrecy provided the supply side.

The same is true of the much bigger problems of tax evasion and organised crime. These activities are enabled by the network of secrecy suppliers: the offshore financial centres and the pinstripe infrastructure of bankers, accountants and lawyers who create secretive structures and help clients navigate secrecy jurisdictions for a fee. It is time to turn the spotlight onto the supply side of corruption, especially those jurisdictions which prosper by providing a safe home for illicit financial flows.

The Second Wave

The FSI ranks the world's secrecy jurisdictions. In doing so, it is the first crest of a 'second wave' of understanding corruption, which acknowledges the wider problem of illicit financial flows. In turn, the supply side of illicit financial flows is finally brought under scrutiny. Tackling the global menace of dirty money means acknowledging the existence of secrecy jurisdictions, and taking action to curb their illicit activities. The FSI shows us where to start.

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