



# COMMENTARY

Center for Strategic and International Studies ■ Washington D.C.

## **Abetting Poverty, Drugs, and Terrorism: Illicit Financial Flows**

By Gerald Hyman, President, Hills Program on Governance

July 9, 2007

Most of the discussion on development, especially for Africa, assumes that there are rich countries and poor countries and that development requires that the rich countries provide more funding and assistance to the poor ones. That may be so. Less understood by far, however, is the amount of money conveyed annually from the poor countries to the rich ones through illicit financial transactions: funds that are illegally generated, transferred, or used.

On June 28, at a conference co-sponsored by the CSIS Hills Program on Governance and the Global Financial Integrity Program at the Center for International Policy, nearly 200 participants gathered at CSIS to discuss what is known about these flows, how they are generated, how they work, how they affect development, and what can be done to reduce them. A conservative estimate of illicit cross-border flows – inherently an estimate because these are, after all, illicit flows – is that they amount to between \$1 trillion and \$1.6 trillion annually, and \$500 billion to \$800 billion of that amount (around 50 percent) is conveyed each year from poor countries to rich ones. That is 8 to 10 times the amount of official development assistance (ODA) provided by the rich countries to the poor ones, and much of ODA is in the form of salaries and other expenses paid for “technical assistance” to citizens of the rich countries.

The mechanisms for generating illicit funds include, but are hardly limited to, under-pricing exports or overpricing imports (and pocketing the difference), falsifying transactions entirely, evading taxes, multiplying books, creating false trusts with hidden beneficiaries, and working through dummy corporations, offshore entities, tax havens, money-laundering fronts, and the like. Bribery, corruption, kickbacks, and forgeries grease the flows. A web of financial intermediaries now in dozens of countries conceals the flow through mazes of fake paperwork transactions. Through this web of false financial transactions, the natural resources and the value added by dozens of the poorest countries are turned into bank accounts, mansions, and gold. It is a massive transfer of scarce resources, perpetuates the poverty of those who produce the goods and resources, and is made possible by acts of omission and commission in the industrialized world.

The receiving countries permit the deposit of income from international activities that they criminalize when those acts are committed domestically. Indeed, in the domestic context even the receipt of income from such activities is itself criminal as accessory to the underlying crimes. Yet, many countries do not criminalize them when they are international and even subsidize them through tax deductions. Some countries even specialize in, and make good money from, creating the secret accounts, tax havens, anonymous trust accounts, fake foundations, and the like, which constitute the financial structure that enables, even supports, these illicit flows. According to Raymond Baker (perhaps the foremost expert in the area and the intellectual parent of the GFI/CSIS Hills conference), criminalizing such transactions from abroad would release more funds to the poor countries – allow them to be retained, actually – than the combined proceeds from free trade, export promotion, economic assistance, and foreign assistance.

Leaving aside, however, any altruistic impulses to help the poor and the effects of illicit financial flows on their poverty, the “exploratory” work done for their own benefit by the “giants” of this field – Mobutu Sese Seko, Ferdinand Marcos, Sani Abacha, for example – have provided lessons to others with even more nefarious incentives. After all, Mobutu, Abacha, and Marcos merely wanted to capture for themselves the proceeds from otherwise legal, sometimes even laudatory activities. They wanted to be rich and live among their kind.

The pathways they pioneered, however, are now traveled by drug smugglers and terrorist financiers as well. Those like Osama bin Laden were quick to learn the lessons and apply them. Whatever one may think of the conversion of legal activities for personal benefit through what would be illegal if they were done here, it is a different matter when the underlying activities themselves, not just the means of conversion, are human trafficking, drug production and distribution, weapons smuggling, counterfeiting, theft, and forgery, to name only some of the mechanisms. That chain harms the citizens of the rich countries, not merely the poor ones.

To the extent that our legal and financial structures abet terrorists and drug bosses, it may now be more than a matter of altruism to plug these illicit transactions. It may now be a matter of our health and national security as well.

*The Center for Strategic and International Studies (CSIS) is a private, tax-exempt institution focusing on international public policy issues. Its research is nonpartisan and nonproprietary. CSIS does not take specific policy positions; accordingly, all views, positions, and conclusions expressed in these publications should be understood to be solely those of the authors.*