

11. Effectiveness: threat and corresponding policy response

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11.1 INTRODUCTION

Chapters 3 to 10 have described the different aspects of AML/CTF policy in detail. These chapters show that AML/CTF policy has quite a lot of different and important elements that, together, represent the total policy response. In this chapter we try to bring all this information together in order to explore to what extent the policy response towards money laundering is effective in relation to the money laundering threat the country is facing, which was calculated in Chapter 2.¹

11.2 METHODOLOGICAL APPROACH

Since AML policy has such multiple and varied dimensions, which cannot be encompassed in a single measurement of policy response without great loss of accuracy, we select the most suitable indicators for a good policy response. We therefore plot these indicators, one by one, next to the ML threat to explore how these two variables are related. The suitable indicators analysed in this chapter represent AML policy and have a logical hierarchy and are furthermore selected based on data availability and cross-country comparability. It is conceptually hard to compare an indicator for AML policy with threat estimation because the units of measurement are by definition completely different. The visual exploratory approach we use in this chapter can indicate whether the policy

¹ Note that our analysis focuses here on money laundering only. There is insufficient data on terrorist financing to perform a similar analysis for terrorist financing at this point. However, the same methodology could be applied in the future when more data on terrorist financing policy is available and when we have more insight into what determines the threat of terrorist financing in the different EU Member States.

response is proportional, but cannot be seen as an exact measurement.² The exploratory analysis is based on a figure which has along the horizontal axis a policy response indicator (in which a higher score is a better policy response), with threat (either in millions of Euros or as a percentage of GDP) on the vertical axis. We consider the diagonal area in this figure an appropriate policy response in the sense that a country in this area has a policy response that is more or less proportional to the threat it is facing. Member States that are plotted in the bottom-right-hand corner are playing safe, since their policy response is more than proportional to the threat they are facing. We consider countries plotted in the top-left-hand corner to be at risk of having a less than proportional policy response.

11.3 THE SELECTED INDICATORS FOR POLICY RESPONSE

We selected the following variables to represent the policy response: FATF compliance score, legal effectiveness score, timeliness of implementation, FIU response score, international cooperation score, information flow score and the number of convictions for money laundering. We give a small overview of these indicators, which elements of AML policy they cover, how they are measured and what their downsides and merits are.

FATF Compliance Score

Our first indicator for policy response is an FATF compliance score, because these recommendations were actually the starting point for our research. The FATF/MONEYVAL evaluate all countries on the extent to which they are compliant with each of the 40 FATF recommendations. In constructing the FATF compliance measure we simply added up the scores for each recommendation (by giving 3 points when a country is fully compliant, 2 when it is largely compliant, 1 when partially compliant and 0 when non-compliant), based on the latest Mutual Evaluation Report for each country. The advantage of using FATF compliancy scores is that they are available for all Member States and that all Member States are scored on the same basis. The downside of this measure is that national

² The results of our analysis are for instance sensitive to the scaling of the axes and are primarily a relative score. We therefore made all indicators for AML policy response take only positive values, with the characteristic that more is always better, and have (0,0) at the origin (bottom-left-hand corner) of the graphs.

scores come from different time periods (some are almost ten years old), are being awarded by different teams, offer mainly a measure of ‘law in the books compliance’ and not of ‘law in action compliance’, are not completely cross-country comparable,³ and assume that every recommendation is of equal importance in terms of having an effective AML policy – which is obviously not the case. The FATF does not take into account to what extent a country is threatened by money laundering.

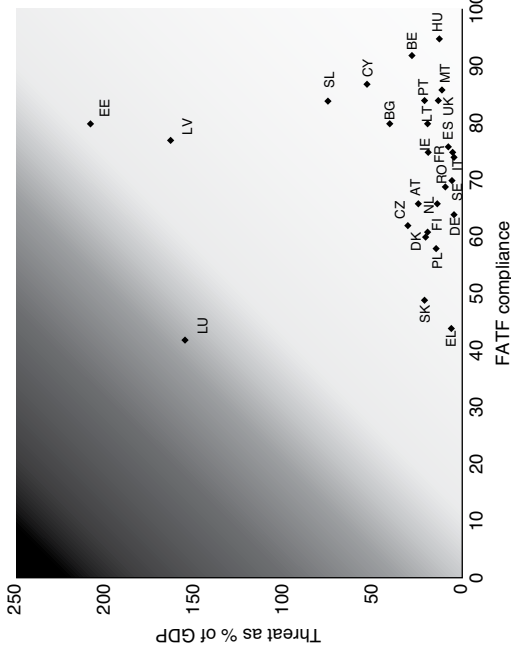
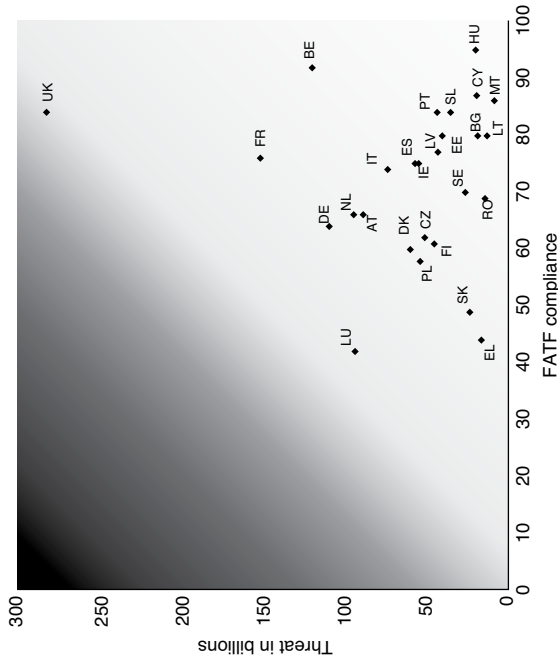
If a country were to be fully compliant with all 40 recommendations of the FATF, it would receive a FATF compliance score of 120 (40 times 3). The 27 EU Member States receive scores of between 42 (for Luxembourg) and 95 (for Hungary). When assessed for threat (see Figure 11.1), none of the EU Member States is in the black zone (at risk). Only Luxembourg, due to its bad compliance score, is in the grey zone, no matter whether threat is measured as a percentage of GDP or in millions of Euros. Latvia and Estonia face a relatively high level of threat (if calculated as a percentage of GDP), but are nonetheless in the grey zone due to their relatively good compliance score. The same holds for UK when threat is measured in millions of Euros.

Legal Effectiveness in Preventive AML Policy

Our next indicator is a measure of the legal effectiveness of the substantive norms in preventive AML policy. This indicator is based on the analysis in Chapter 3 of this book. In Chapter 3 we identified, besides the general factors that negatively influence the legal effectiveness of Member States’ AML/CTF policies, a number of potential legal hindrances to preventive AML policy for each Member State. We constructed an index of legal hindrances for every country using the following weights: 1 for technical hindrances, 3 for fundamental hindrances and 2 for other hindrances. We were then able to create a scale of legal hindrances across the European Union using this indicator. The scale was proven not to be overly sensitive to the chosen weights. As a last step, we took the inverse of this legal hindrance measure to obtain the legal effectiveness measure presented in Figure 11.2 and in online appendix 11.2 at <http://goo.gl/VZgJb3>.

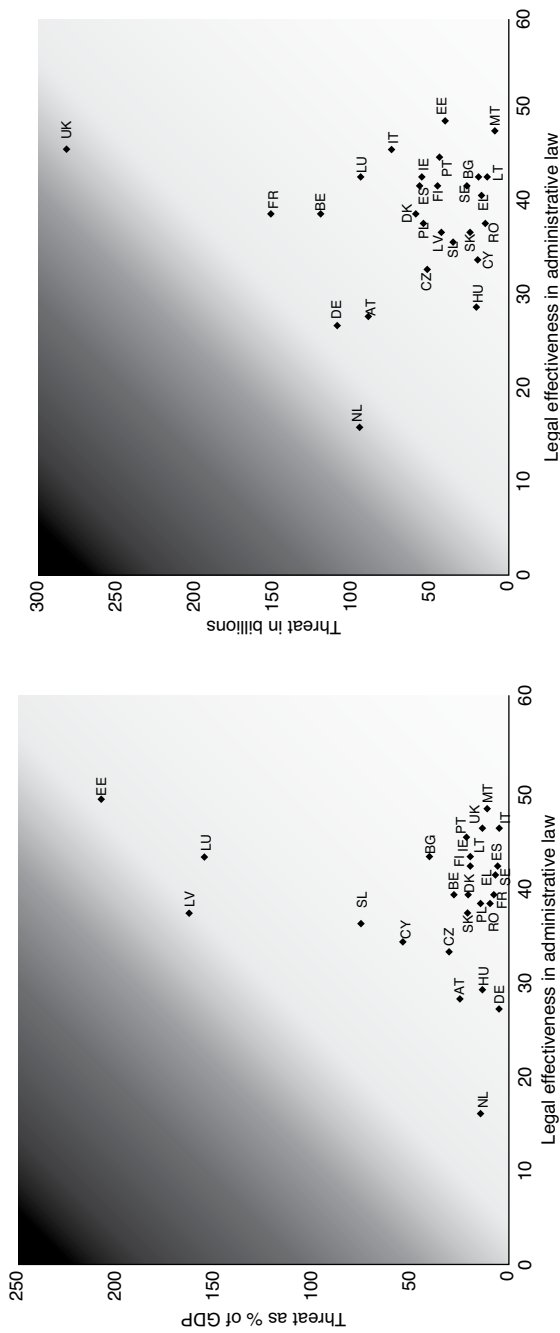
The advantage of using such a measure is that it is easily constructed once one has identified the legal hindrances present in the preventive

³ A member of a FATF evaluation team has indicated that the situation of the country (like the state of its economy) is considered when giving the compliance score. This would mean that a poor country could get a rating of largely compliant for a certain recommendation, while a richer country with the exact same policy might get a rating of only partly compliant.



Source: Created by the authors, based on the following data: for threat estimations, see Chapter 2; the FATF compliance score is a simple addition of the compliancy scores given by the FATF for the different recommendations. To make this addition possible we transformed the scores into numbers. Fully compliant = 3, largely compliant = 2, partially compliant = 1, non-compliant = 0 and not applicable = 3 (because N/A is usually given where the recommendation is not necessary; for example, in countries where trusts are not permitted, there is no need to comply with recommendation 34; legal arrangements are beneficial to owners, so it is as good as fully compliant). Online appendix 11.2 lists the exact scores for all Member States (see <http://goo.gl/VZgJb3>).

Figure 11.1 Visual representation of threat vs. FATF compliance score



AML policy of the Member States. The disadvantages are that it is a crude exercise in translating qualitative into quantitative information, the weights attached to each of the hindrances are open to discussion and also that the categorization of hindrances has a direct effect on the index as well as an indirect effect on the country rankings. Furthermore, there is a lot of data asymmetry between the Member States. First, for some Member States there is a lot more information publicly available than for other Member States. Second, for some Member States the information available was far more outdated than for other Member States. For example, some FATF or MONEYVAL evaluations date from 2006. In the case of Member States for which more and more recent information is available, we also know more about hindrances. This generally means they end up with a lower legal effectiveness score. We acknowledge this methodological issue.

The Member State identified as having the least legal hindrances was Estonia, which obtained a score of 49 out of a maximum of 50. Having had a very recent FATF evaluation, the Netherlands was the Member State where we were able to identify most legal hindrances. The Netherlands received a score of 20. We took into account that there could be many more hindrances that were overlooked which is why the Netherlands is not considered to be a country with a nil legal effectiveness policy indicator (see Figure 11.2). When compared with our measures of threat, we see that, despite having a potentially excellent preventive legal framework, Estonia's policy response is only proportionate to the threat of money laundering when seen as a percentage of GDP. Similarly, Luxembourg and Latvia seem to have a proportional policy response, whereas all other Member States have taken more than proportional measures to ensure the legal effectiveness of their preventive AML policy given the threat of money laundering they face as a percentage of their GDP. Figure 11.2 also shows that Member States with a strong legalistic background have a proportional and somewhat less than proportional policy response when looking at threat in billions of Euros. This has to do with the fact that these countries are also the most threatened economies.

Third EU Directive Implementation Timeliness

Our next indicator is to what extent the Third EU Directive was implemented on time. Chapter 4 discusses implementation delays in detail; here we use this information as an indicator for AML policy response.

The advantage of this indicator is that it is easily obtainable, easy to calculate and available for all 27 EU Member States. The disadvantage is that implementation delays do not necessarily represent any resistance

or inefficiency on the part of a certain country, but could have quite basic and pragmatic causes, such as delays caused by a change in parliament.

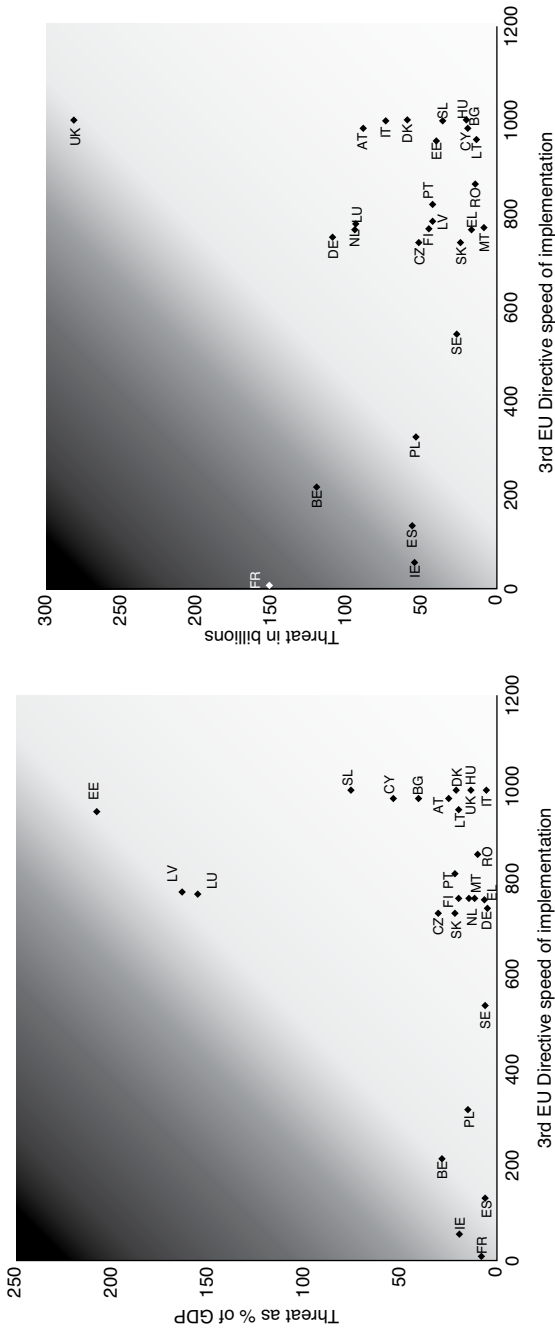
Figure 11.3 shows that France is most at risk (in the black zone) for this indicator, mostly due to the fact that it has the highest implementation delay in the EU: 991 days. The small Member States with a relatively high amount of threat (when measured as a percentage of GDP: Estonia, Latvia and Luxembourg) were relatively fast with the implementation, which is a proportional policy response in our Figure 11.3. Next to France, Belgium is the only country that also has a less than proportional policy response, mainly due to a relative high implementation delay of more than two years.

AML FIU Policy Response

In constructing the AML policy response indicator for the FIU we made use of a factor analysis using several indicators described in Chapter 7 of this book: the FIU budget securitization score, the FIU data access score, the FIU feedback score and the suspicion reports receiving and processing score.

The FIU budget securitization measure depends on the FIU's financial independence and is also affected by the type of organization the FIU is accountable to. We operationalize the FIU's budgetary independence by giving 4 points to FIUs who have a completely separate budget which they can administer themselves, 3 points to FIUs that receive their budgets from another organization but are within the first decision tier in the organogram, 2 points to FIUs that receive their budgets from another organization but are within the second decision tier in the organogram and finally, 1 point to FIUs that receive their budgets from another organization and are within the last decision tiers in the organogram. We operationalize the measure of FIU accountability by giving 2 points if the institution to which the FIU is accountable is the national parliament or a ministry and if the organization in charge of appointing the head of the FIU is either the government, the parliament or a ministry, and 1 point if the institution to which the FIU is accountable to is the police or the prosecution office, and when members of these institutions also appoint the head of the FIU.

The data access score is constructed on the basis of the type of access that FIUs have to several databases: direct or on request, online or not (see Table 7.4). Based on the importance that FIU representatives in general gave to direct information access versus online access, we gave 10 points for online direct access – thus recognizing that this is the best form of access, 9 points for direct but not online access – since this form



Source: Created by the authors based on the following data: for threat estimations see Chapter 2; the speed of implementation is calculated by subtracting the implementation delays shown in Figure 5.1 of this report from 1000. The subtraction ensures the x-axis represents a policy response indicator for which more is better; the subtraction from 1000 has the effect of making all scores positive (the maximum delay in the EU is 991 days for France) and therefore we can have (0,0) at the origin (bottom-left-hand corner). Online appendix 11.2 lists the exact scores for all Member States (see <http://goo.gl/VZgJb3>).

Figure 11.3 Visual representation of threat vs. implementation timeliness

of access is only lacking speed, 5 points for indirect access – as more information and time can be lost with this lack of transparency, and no points when the FIU has no formal or informal access to a database.

The suspicion reports receiving and processing score is based on the way reports are received and analysed by the FIUs – by mostly electronic means or mostly manually, and with or without the help of data-mining systems (see Table 7.5). We aggregated this data into three categories for suspicion reporting – high speed (when the Member State representatives suggested that the FIU receives only electronic reports or mostly electronic reports), medium speed (when the Member State representatives suggested that the FIU receives electronic, paper and fax reports) and low speed (when the Member State representatives suggested that the FIU mostly receives STRs as paper copies or by fax). Similarly, for data mining there are two groups: FIUs that have a data-mining/analysis system and FIUs that do not, at the time we conducted this research.

The FIU feedback score is based on whether FIUs provide standard reporting forms to the reporting entities, have helpful websites with readily accessible annual reports where reporting entities can report online, give regular training sessions and workshops and confirm the receipt of a suspicion report (see Table 7.3).

These indices are the results of crude exercises of translating qualitative information into quantitative data and are also subject to data asymmetry between the Member States. In order to reduce these disadvantages, we used a factor analysis method to construct a general measure of FIU AML response. A description of the factor analysis can be found in online appendix 11.1. The advantages of this method are that it takes away some of the variation in these indices which could be due to either index construction or data availability, and that it allows for cross-country comparability across all of the FIUs of the European Union.

According to this factor analysis, the Italian FIU has the lowest policy response which means that it has a proportional policy response if threat is measured as a percentage of GDP and a less than proportional policy response when threat is measured in billions of Euros. Similarly, the UK FIU has an under-proportional FIU response, although this is mostly due to the high threat its economy faces.

International Cooperation Score

Money laundering is for the most part an international crime, which makes international cooperation in the fight against money laundering an important element. Chapter 9 of this book analyses the international cooperation of the 27 EU Member States in the form of the signature,

ratification and implementation of the principal international conventions in the AML/CTF field. This overview is the basis for the construction of the policy indicator for international cooperation that we analyse here. Signature of a convention is awarded 3 points, ratification 2 points and full implementation 1 point. The total maximum score is 33 points, based on 6 points for the Vienna Convention, UN Terrorist Financing Convention and Palermo Convention and 5 points for CoE 1990, the Merida Convention and CoE 2005 (NB: full implementation is only analysed for the Vienna, the Terrorist Financing and Palermo Conventions).

This indicator is available for all Member States and is straightforward to calculate, but the disadvantage of this indicator is that it only shows 'compliance in the books', which might be quite different from actual performance in international cooperation.

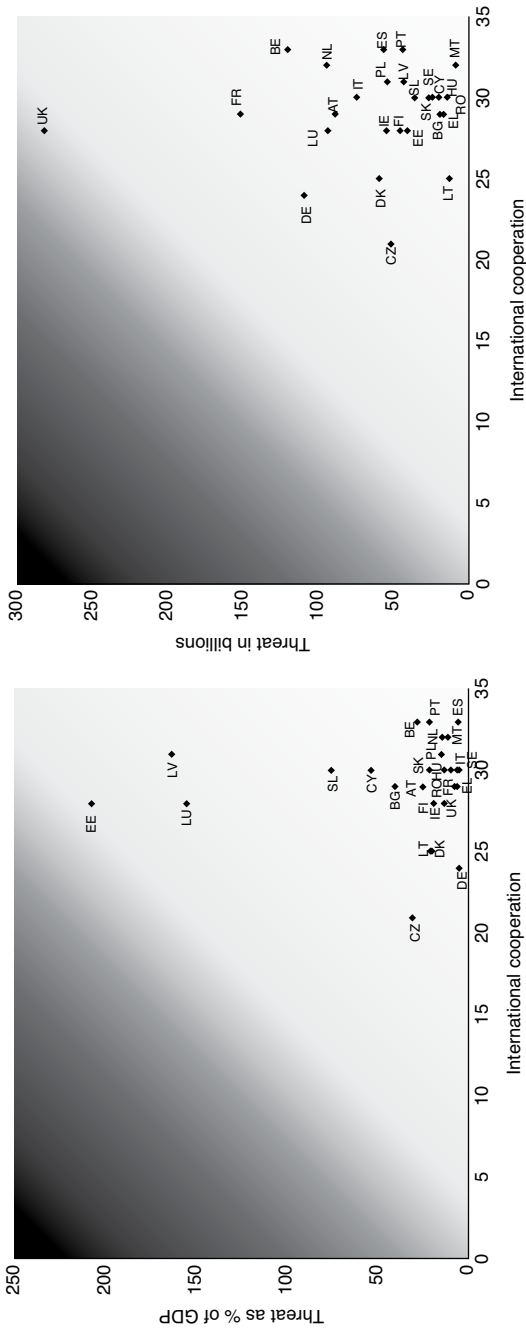
Due to the relatively high scores for international cooperation by the EU Member States, most countries are in the white zone and, hence, on the right-hand side. Only Estonia, Luxembourg and the UK are in the grey zone due to their relatively high levels of threat (either measured as a percentage of GDP or in billions of Euros).

AML Information Flow Scores

In constructing the information flow score, we could not rely too much on statistics, since there are virtually no such statistics available across the EU. This measure was constructed on the basis of the four types of information transmission chains that were identified in each country in Chapter 8, correcting for additional information transmission mechanisms (such as double reporting and liaison officers). We further used government effectiveness and corruption perception indicators available for all the EU Member States as proxies for the two types of identified information loss described in the value of the network calculations – limited interaction and deviant interests, respectively.

The advantages of this policy response indicator are the cross-country comparability and the identification of best practices in information transmission within a country. The disadvantages are that there is a great deal of data asymmetry across the Member States, that the proxies used for information decay may not reflect the different information decay that may occur when investigative agents cooperate and that these models are overly simplified and do not take into account other types of barriers to criminal apprehension (such as resources, priorities of the law enforcement entities).

The maximum information flow score occurs in a star information flow chain with the best corruption perception and government effectiveness



Source: Created by the authors, based on the following data: for the threat estimations see Chapter 2; for the international cooperation score see Chapter 9. See online appendix 11.2 lists the exact scores for all Member States (see http://goo.gl/VZ_gJb3).

Figure 11.5 Visual representation of threat vs. international cooperation

scores and in our sample they vary between 233 (Denmark) and 7.7 (Romania). Despite the large differences in the information flow scores, most countries have proportional policy responses considering the money laundering threat levels they are exposed to (see Figure 11.6). Exceptions are the small countries with a high exposure to threat as a percentage of GDP – Estonia and Latvia and the large financial centres such as the UK, when threat is expressed in billions of Euros. For Italy, the information flow scores reveal that national cooperation in AML matters may be under proportional to the threat, if this is expressed in billions of Euros.

ML Convictions

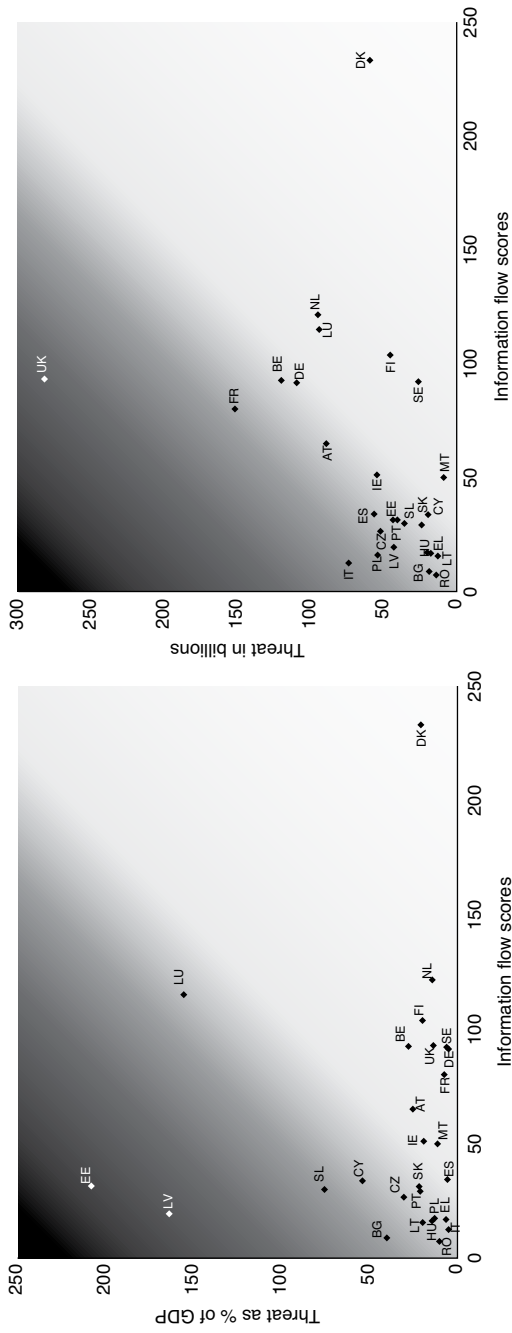
One of the goals of anti-money laundering policy is of course to catch money launderers and convict them. We therefore see the number of money laundering convictions as one of the most important indicators measuring the result of anti-money laundering repression policy, even though cross-country comparability is still dubious, as mentioned extensively in Chapter 10.

Denmark has a relatively high number of money laundering convictions per year and relatively low levels of threat (both measured in billions and as a percentage of GDP) and is therefore the only country that is on the safe side (in the white zone) in both graphs. Although the UK has by far the most convictions per year, when compared with the threat it is facing (measured in billions of Euros), this policy response is only proportional.

11.4 RESULTS

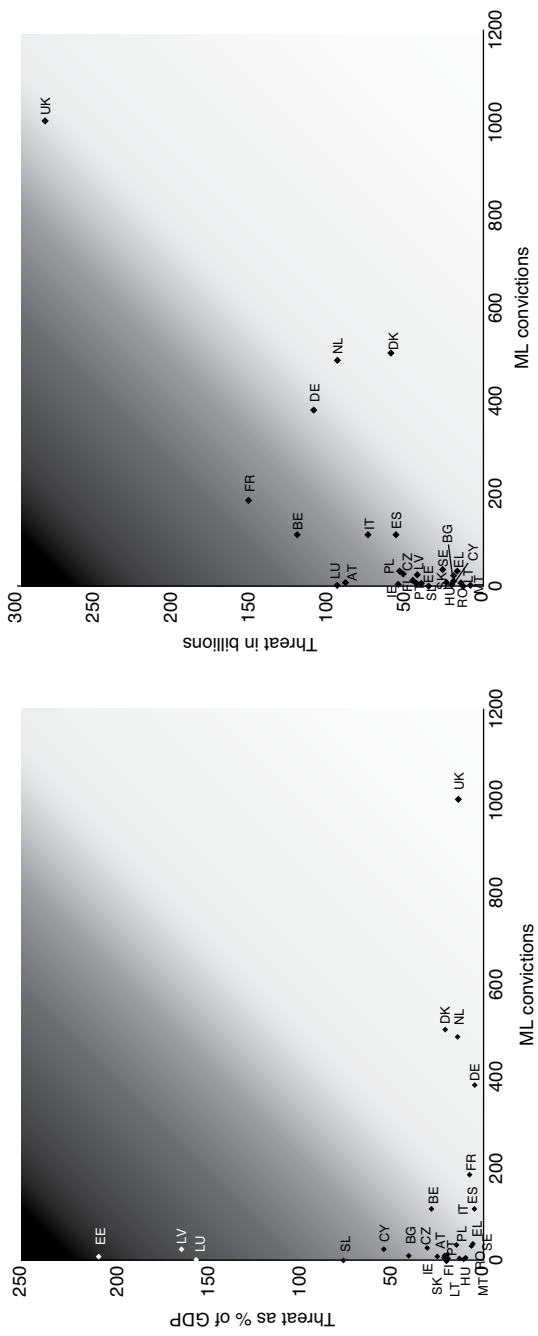
When plotting and analysing the results for all Member States of our visual exploratory approach for all our selected indicators for the policy response, we can identify for each country whether their policy response is either over-proportional (white), proportional (grey) or under-proportional (black) for each part of the policy response. These results are shown in Table 11.1.

As can be seen from the table, Denmark is the only Member State that is fully in the white zone – hence, on the safe side – for all the indicators of policy response both in relation to threat measured as a percentage of GDP and measured in millions of Euros. Not only does Denmark have a relatively low amount of threat, it also scores quite well for all the indicators we selected. Remarkably though, Denmark has been criticized by the FATF for not criminalizing self-laundering. Our analysis does not indicate that this severely limits their ability to fight money laundering.



Source: Created by the authors, based on the following data: for the threat estimations see Chapter 2; for the information flow score see Chapter 8. For Estonia, Denmark, Finland, Lithuania and Sweden, the analysis of the information flow chains was performed at a much more superficial level than for the other Member States, due to the timing of our research. Furthermore, information flows in the UK will change in the near future. See online appendix 11.2 lists the exact scores for all Member States (see <http://goo.gl/VZg1b3>).

Figure 11.6 Visual representation of threat vs. information flow score



Source: Created by the authors, based on the following data: for the threat estimations see Chapter 2; the data used to calculate the average number of money laundering convictions per year in the period 2005–10 is specified in Chapter 10. See online appendix 11.2 lists the exact scores for all Member States (see <http://goo.gl/VZg1b3>).

Figure 11.7 Visual representation of threat vs. number of ML convictions

Table 11.1 Overview of the extent to which the policy response of EU Member States is proportional to the threat

	Threat as % of GDP vs. FATF compliance score	Threat in millions vs. FATF compliance score	Threat as % of GDP vs. Legal effectiveness	Threat in millions vs. Legal effectiveness	Threat as % of GDP vs. Implementation timeliness	Threat in millions vs. Implementation timeliness	Threat as % of GDP vs. FIU response score
AT	W	W	W	G	W	W	W
BE	W	W	W	W	G	B	W
BG	W	W	W	W	W	W	W
CY	W	W	W	W	W	W	W
CZ	W	W	W	W	W	W	W
DK	W	W	W	W	W	W	W
EE	G	W	G	W	G	W	G
FI	W	W	W	W	W	W	W
FR	W	G	W	G	G	B	W
DE	W	G	W	G	W	W	W
EL	W	W	W	W	W	W	W
HU	W	W	W	W	W	W	W
IE	W	W	W	W	G	G	W
IT	W	W	W	W	W	W	G
LV	G	W	G	W	G	W	G
LT	W	W	W	W	W	W	W
LU	G	G	G	W	G	W	G
MT	W	W	W	W	W	W	W
NL	W	W	G	G	W	W	W
PL	W	W	W	W	G	G	W
PT	W	W	W	W	W	W	W
RO	W	W	W	W	W	W	W
SK	W	W	W	W	W	W	W
SL	W	W	W	W	W	W	G
ES	W	W	W	W	G	G	W
SE	W	W	W	W	W	W	W
UK	W	G	W	G	W	G	W

Source: Created by the authors, based on indicators developed in the ECOLEF project. See online appendix 11.2, <http://goo.gl/VZgJb3>, for a description of how we establish each ranking. W = the white zone, which indicates that a country is on the safe side by having an over-proportional policy response to the threat it is facing, G = the grey zone, which indicates that the policy response is more or less proportional to the threat and B = the black zone, which indicates that the Member State might be at risk due to having an under-proportional policy response to the threat it is facing.

Threat in millions vs. FIU response score	Threat as % of GDP vs. Information flow score	Threat in millions vs. Information flow score	Threat as % of GDP vs. International cooperation score	Threat in millions vs. International cooperation score	Threat as % of GDP vs. Number of convictions	Threat in millions vs. Number of convictions
W	G	G	W	W	G	B
W	G	G	G	W	G	B
W	G	G	W	W	G	G
W	G	G	W	W	B	G
W	G	G	W	W	G	G
W	W	W	W	W	W	W
W	B	G	W	W	B	G
W	G	G	W	W	G	G
W	G	G	W	W	G	B
W	G	G	W	W	G	G
W	G	G	W	W	G	G
W	G	G	W	W	G	G
W	G	G	W	W	G	G
G	G	G	W	W	G	G
G	G	B	W	W	G	G
W	B	G	W	W	B	G
W	G	G	W	W	G	G
W	G	G	G	W	B	B
W	G	G	W	W	G	G
W	W	G	W	W	W	G
W	G	G	W	W	G	G
W	G	G	W	W	G	G
W	G	G	W	W	G	G
W	G	G	W	W	G	G
W	G	G	W	W	G	G
W	G	G	W	W	G	G
W	G	G	W	W	B	G
W	G	G	W	W	G	G
W	G	G	W	W	G	G
B	G	B	W	G	W	G

For the rest of the Member States we see in general quite a mixed picture, with most countries ending up in the grey zone for some indicators, while being on the safe side (in the white zone) for most of the indicators. None of the Member States ended up consistently in the black zone. Actually,

the Member States that ended up most in the black zone did so only twice (out of the 14). Estonia ended up least in the white zone, simply because – according to our estimations – the country is so much threatened by money laundering, especially when it is measured as a percentage of their GDP. This is the result of a relatively small country (Estonia) being located next to a very big country with a significant amount of crime and, therefore, criminal proceeds (Russia).

11.5 CONCLUSION

One of the critiques of the FATF mutual evaluations is that they do not take into account to what extent a country is threatened by money laundering. In this chapter we explore to what extent the policy response of the EU Member States relates to the size of the money laundering threat it faces. To do so, we mapped all Member States in a graph with threat and a policy response indicator on the axes. In our analysis, countries with high levels of threat and a relatively weak policy response end up in the black zone, which we typify as being at risk, because the policy response is under-proportional. The countries with low levels of threat and a relatively strong policy response end up in the white zone, which we typify as being on the safe side, because the policy response is over-proportional. When the policy response is more or less proportional to the threat, countries end up in the grey zone. This visual exploratory approach shows that most EU Member States are generally on the safe side (in the white area), with only a few Member States ever ending up in the black zone. Although the EU Member States perform relatively well in our analysis, almost all of them can improve on certain indicators. The positive exception here is Denmark, which has been criticized by the FATF for not criminalizing self-laundering, but which in our analysis has not only relatively low levels of threat, but also relatively good scores for all our policy response indicators.