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Chapter x

The Monty Python Flying Circus of Money Laundering and the Question of Proportionality

Petrus van Duyne, Jackie Harvey and Liliya Gelemerova

"*I'm sorry to have kept you waiting, but I'm afraid my walk has become* rather sillier recently."
Monty Python's Flying Circus:
The Ministry of Silly Walks[1]

Introduction: proportionality and global AML policy

One does not need to be a moralist to recognise the moral function of the state as an actor protecting against harm. Since times immemorial this has given the responsible authorities huge powers that seem to have a built-in justification: 'We act for the common good' which implies serving and protecting society against harm. And what is harm to society? Naturally, that depends on the two sides of the equation: society and harm. Though this appears a self-evident truth, looking closer the truth value soon evaporates as both concepts prove to be ill-defined and, therefore, boundless. In particular, the concept of harm has no boundaries. What does it encompass? Physical safety, war, public disorder and health seem to be sufficiently delineable, but as soon as one addresses aspects other than (physical) health and harm, boundaries become faint and inconsistent, if not arbitrary. And so are the related policies pursued to fend off alleged threats to such ill-defined aspects of the common good.

This sounds abstract, but has hard and tangible consequences. History abounds with examples of rulers who took their task of protecting society against harm so boundlessly that the cure was worse than the alleged threat, in particular, when spiritual values were at stake. One does not need to go as far as the Spanish Inquisition, which protected society against the threat of heresy, to recognise the effects of 'boundless protection'. Indeed, there are sufficient examples of lofty societal protection policies that to the degree in which they lack proper limitations,

[1] Monty Python's Flying Circus ran on BBC TV from 1969 to 1974. This quotation is taken from: http://www.telegraph.co.uk/comedy/comedians/monty-python-s-25-funniest-quotes/ (accessed 9/10/2015).

drift to an all-encompassing implementation and in due course become insensitive to the principle of proportionality. More recent examples can be found in regard to certain aspects of the global policies of drugs (ab)use, organised crime and terrorism in which we find a constant shifting and blurring of the boundaries of implementation (Van Duyne and Levi, 2005; Ruggiero, 2003; Hobbs, 1998) wherein a serious threat presentation justifies extraordinary 'serious' laws. Thus, in the UK the Proceeds of Crime Act (2002) and the Serious Crime Act (2007) enable the courts to impose heavy inroads against individual freedoms through restrictive conditions around work, travel and finances for those involved[2] even in the absence of conviction. This is amplified by the state of technique, which allows the state an ever increasing (and intrusive) monitoring of citizens, all for the general good encompassing any kind of (un)safety. Technique is neutral and knows no balancing against other interests.

This balancing of interests matters. Policies that entail (financial and political) costs to society must be addressed from a proportionality perspective. This is the more important if such policies demand special additional efforts or intrude into human and citizens' rights and liberties. By its nature, criminal law policy has such an intrusive character which must therefore be balanced according to the principle of proportionality, even if this balancing sometimes slips into ritual formulations.[3]

The principle of proportionality should not only play a role in criminal policy, but also in adjacent regulatory policies. One such adjacent field is the global anti-money laundering policy, of which the criminal and regulatory components are strongly connected. For this reason the focus of this chapter is to examine the role of the proportionality principle in the field of Anti-Money Laundering (AML).

Elements of proportionality and AML policy: twin scales

The concept of proportionality permeates the whole legal sphere but for practical application is clearly in need of operationalisation: it supposes a clear equilibrium, which is not a priori given. This also applies to the field of AML policy: operationalisation of the concept is difficult although no one pleads to declare it irrelevant. However, making the proportionality principle concrete in its application cannot be achieved by a sweeping general formula. Instead, we have to look at elements in the AML policy that at first sight are relevant for determining proportionality. For each element we have to ask the question: 'Can it be specified

[2] Through application of serious crime prevention orders.

[3] Jacobs, F.G., Recent Developments in the Principle of Proportionality in European Community Law, in: The Principle of Proportionality in the Laws of Europe, 1999, p. 2. Christoffersen, J., Fair Balance: Proportionality, Subsidiarity and Primarity in the European Convention on Human Rights, 2009, p. 31.

sufficiently for a proportionality equation?' We can also use the metaphor of the balance with two scales which must be filled concretely for properly weighing one against the other. For example, the threat of money laundering must be balanced against the countermeasures. This is a many faceted issue requiring a step-by-step analytical and empirical process, albeit, without subsequent guaranteed success.

a. The crime-money (and laundering) threat side of the balance

The term 'money laundering' is a technical construction but not a neutral one. As long ago as 1998, van Duyne indicated that it was exploited for political ends and provided with emotional meanings by what he termed the "threat assessment industry" (p. 359; see also Verhage and Ponsaers, 2009). This is particularly the case if it is connected with the concept of '(transnational) organised crime' (Van Duyne and Nelemans, 2011). Thus we see enshrined in the supra-national regulations statements that money laundering (and terrorist financing) "shakes the very foundations of our society".[4] Threat is indeed the first and most important relevant element to consider for balancing: politically it is the most mentioned reason for AML policy.

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More important, the threat of crime-money is also a better candidate variable for a proportionality equation than a general moral imperative, such as 'crime should not pay'. A moral statement expresses an absolute or dichotomous value about an act such as law breaking: it is there or not. A threat is, in principle, a scalable phenomenon for 'putting on the scales' of a balance. While this sounds simple, problems arise in determining exactly what should be added to the scales. That should be a solvable puzzle as every insurance expert knows: on one scale is the harm, on another the financial compensation. However, even an insurance comparison of two similar threats makes clear that nothing is self-evident. For example, New Orleans (USA) and the Western Netherlands both consist of lowlands and are always threatened by flooding. How to convert that threat proportionally into another variable: the size of the protecting dikes? That requires weighing other interests. The authorities of the two areas found two relevant but different 'weights': value of physical assets versus value of human lives. In New Orleans protective dikes were constructed in proportion to the value of protected assets, which entailed that mainly poor neighbourhoods (considered low valued assets) were flooded with loss of life of (mainly poor) citizens. In the Netherlands the threatened interest is the human life which implies dikes of an equal defence quality for all. Indeed, nothing is self-evident: the same water and potential

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[4] Directive 2005/60/EC 26th October 2005 (page 1) on 'the prevention of the use of the financial system for the purpose of money laundering and terrorist financing', available from http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32005L0060 (accessed 19/10/2015).

flooding, but different threats and responses. Does this also apply to the AML policy?

Almost 30 years ago IMF Managing Director Camdessus stated that the threat of money laundering was "2 to 5 percent of global GDP . . . probably [as] a consensus range".[5] Underlying evidence for this 'consensus range' was not provided, nor was it clear between whom such consensus existed. Notwithstanding such absence of fact, Tanzi (1996) and Quirke (1996) of the same Institute hastened to provide some substantiation. But where did that threatening crime-money come from? To provide a proxy-variable for money-generating crime they resorted to the crime-data from Interpol though seemingly without judging its (un)reliability for this purpose. Next they used a broad definition of money laundering, which is tantamount to the (hypothetical) sum of transactions in the shadow economy, particularly if tax crimes are included (Gelemerova, 2011).

This was an approach which conveniently fitted into the statement of the IMF hierarchy. Given the authority (and power) of the IMF it was adopted by the UNODC. In its report, the UNODC estimated the amount of crime-money (proceeds) at $ 2.6 trillion ~~yearly~~ in 2009 of which $ 1.6 trillion would be 'available' for laundering (UNODC, 2011). The term 'available', a phrase with unspecified meaning, was adopted from the 1990 FATF report.[6]

Many academics eagerly jumped on the bandwagon or aligned themselves with the IMF-led mainstream, and have commented upon the justification for the anti-money laundering regime to protect society, the financial industry and the economy against profit driven crime and connected laundering, albeit sometimes with a sceptical voice (Blickman, 2010; Unger, 2007; Bosworth-Davies, 2008; Levi and Maguire, 2004; Gelemerova, 2011; Arnone and Borlini, 2010; McCarthy et al, 2014; Harvey, 2004; Alldridge, 2003; Soudijn, 2009).

It should be observed that there are few independent empirical sources: as a matter of fact there is much 'reference recycling'. The FATF 1990 report uses United Nations sources for estimations (qualified by the FATF in that report as "of doubtful reliability" (p. 5)) while the UNODC (2005) uses again the FATF 1990 estimates as a source. There are also no independent sources used which are outside the 'IMF consensus' while it is apparent that nobody knows how this consensus emerged. Walker and Unger (2009, p.823) note that the figure is a complete guess and that it has not been replicated *"even by academics doing intensive studies within the Fund"*. Despite this, Walker and Unger accept the IMF approach and most of the assumptions underlying this guessing 'consensus'. Others

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Both changed

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Added in the 2005 reference

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5 A copy of the speech is available at http://www.imf.org/external/np/speeches/1998/021098.htm (accessed 20/10/2014).

6 The FATF report was even more careful and used the formulation: *"could be available for laundering"* (p. 5). This subjunctive plus the undetermined phrase 'available' was soon converted into the indicative mode: is being laundered.

have drawn attention to the reliance that has and continues to be placed on what, therefore, amounts to inaccurate or flawed data: “Most literature on money laundering effects is pure speculation, or it is based on figures that are either wrongly cited, misinterpreted or just invented” (Barone and Masciandaro, 2011, p. 118; see also Blickman, 2010; and Schneider and Windischbauer, 2008).

The attempt by the UNODC (2011, p. 79) to come to more sophisticated estimations is marred by its heavy reliance on the ‘IMF-consensus’, the maintenance of which seems to be a holy task, while it is loaded by an accumulation of assumptions. For example, that money “available for laundering” would have an income threshold of US$ 18,000[7] (to be discussed below). Below that threshold, money would simply be spent without laundering (though, according to the definition of the Council of Europe this is technically laundering too). Based on our prior research on more than 150 organised crime cases (Van Duyne et al, 1990; Van Duyne, 1995; Meloen et al., 2003) and of confiscation and asset recovery databases (Van Duyne et al., 2009; Harvey and Lau 2009; Van Duyne et al., 2014; Harvey 2014), we can state that this is an unrealistic assumption. Based on a preliminary research on criminal money management (Van Eekelen, 2000) researchers of the Dutch Criminal Intelligence Unit decided to set the threshold for research on crime-money at € 450,000 (at that time 1,000,000 Dutch guilders) for the simple reason that below this level there is little, if any, interesting laundering activity to be observed. The upper limit of such expenses was randomly set at the median of the GDP (the 50% point): criminal income above that median was considered to be laundered. This has no empirical basis: it is a recurrent finding that criminal income distribution has a median of around € 5,000 (Van Duyne and Soudijn, 2010). Also, the seepage of money due to criminal lifestyle which require no laundering activities is substantial (Van Duyne, 2003; Meloen et al., 2003). Given these findings it may be more realistic to set the laundering threshold at between € 100,000 and € 500,000.

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Commented [GM6]: The report gives this figure in euros on page 79 but on page 81 it mentions a US$20,000 threshold. Changed to Euros

Though the word ‘available’ is easily overlooked (perhaps because it is so common: it is one of the most frequent words in the UNODC 2011 report, occurring 168 times), it is important because it should be a key word in the threat operationalisation. As ~~mentioned~~ discussed above, the first FATF 1990 report mentioned that *“*50 to 70% [of proceeds] could be *available for laundering”* (p.5). By its meaning this implies a division between laundered and not (yet) laundered money. This is important as it raises the question of what is threatening: laundered or unlaundered money, with the latter then divided in available or launderable and not-available or non-launderable crime-money? It can be argued that o~~O~~ne subset can be excluded from the scales of the threat balance: laundered money. By its nature it is already within the financial system and therefore has become a (taxable)

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changed

Commented [GM8]: I added this as a subtle change in nuance: we want this to be thought provoking and the readers to see how disproportionate some aspects of AML policies are. But we don’t necessarily want to explicitly say that ‘laundered money is just fine’. Ch\

[7] For the year 2009.

part of the official GDP. One may not like it morally, but practically it poses no more financial threat than other recorded financial assets: due to successful laundering it is accountable, 'traceable' and taxable.

What about the 'unlaundered' monies? Leaving aside whether unlaundered criminal money can technically exist in the first place (hiding proceeds is also laundering, according to the Council of Europe definition), the global dangers coming from proceeds hoarded in socks, mattresses and pillows or from the daily livelihood expenses trickling into the upperworld economy need to be specified. Criminal revenues, whether laundered or hoarded, have always slipped into the licit economy. Historical economic research should bring that to the surface: models must be tested on established historical data, not on the daydreams of scenarios. For example, how were the criminal revenues from bootlegging during the Prohibition era integrated into the US economy and what financial threats could be identified in the 1920s and 1930s?[8]

This short exposé leaves us with an unanswered question: the volume of the threatening phenomenon remains unspecified and we have a concept 'available' that remains undefined. This scale of the proportionality balance appears to be filled with assumptions, unspecified concepts with fuzzy delineations and recycled argumentations. In short: collective hunches elevated to an 'IMF consensus' as is discussed in the next section.

b. A critical survey of attempts to produce evidence

The previous section does not bode well for the various attempts that have been made to give empirical substance to the threat side of the AML policy. Empirical studies are scarce and can roughly be divided into two groups: economists who are more or less consensus following or within the consensus range, and behavioural researchers who primarily test the assumptions of the consensus against observations carried out at the micro level using data from criminal files, law enforcement databases or fieldwork.

Within economic models

In the absence of observable data, economists have tended to resort to construction of hypothetical models. The model has two important aspects: its basis and assumptions. The basis is formed by the definition of the phenomenon: "Money laundering is the process by which illicit source moneys are introduced into an economy and used for legitimate purposes" (Walker, 1995, p.1). This definition has an enormous range of application as it also covers mere spending of crime-money

[8] After the repeal of the Prohibition in 1933 many bootleggers, like Joseph P. Kennedy, the father of President Kennedy (Kessler, 1996), dropped out, settled their IRS problems and went into the newly legitimate liquor trade (Abadinsky, 1994; pp. 94-95).

(including tax crime) if that spending is for legitimate purposes.[9] Oddly, using crime-money for illegitimate purposes, like buying a boat intended for smuggling and paying the 'criminal' crew, would not be laundering. The point of the hidden or 'hoarded' monies remains untouched and is qualified as (self) laundering in most jurisdictions. Another part of the basis of the model concerns the estimated percentage laundered per type of crime, mostly 80%: methodologically debatable (no proper account of the respondents) and empirically unrealistic (Walker, 1995, 2004; Reuter, 2013, p. 227). With so much uncertainty in the basis we conclude that the validity of the model cannot be stronger than that of the basis. Unfortunately, a high degree of followership can be observed if judged by the direct acceptance of the assumptions and statements of the IMF, World Bank and FATF, part of which find their way into economic models (ECOLEF, 2013; Walker and Unger, 2009). These models stagger from the first step onwards mainly due to lack of empirical underpinning. Despite these inadequacies, both the model and findings were re-used in the UNODC 2011 Report. This report, prepared by Thomas Pietschmann (Research Officer, STAS) and John Walker (Consultant), also made use of related estimates from Walker (1995) and Walker and Unger (2009)[10].

It should be noted that definitional fuzziness is also a characteristic of the UNODC Report (2011). The problem of defining is mentioned, but no clear and convincing formal operational definition (money laundering = . . .) is proposed. There is no proper analysis of demarcation issues by which we mean: clarifying what is excluded from the set of laundering. In none of these studies is there an unambiguous choice for a particular operational definition or a proper specification of key concepts such as 'available' (or 'launderable').

Commented [GM9]: On page 79 they do discuss what to exclude from the set of laundering in order to arrive at 'available for laundering' figures. But it is not a very clear and convincing definition.

As noted above, a rather ad hoc demarcation line has been drawn in the UNODC 2011 report whereby the median threshold of criminal income ~~was~~ appears to have been set at € 18,000 dividing (assumed/available) laundering and not-laundering. We will later see how plausible this is. Another approach mentioned in the report would be to subtract an approximated amount of money needed for consumption from the gross domestic product figures. "Amounts earned above such per capita consumption expenditure would be available for money-laundering" (p. 81). Note again the added unspecified adverbial phrase of 'available for' which easily slips towards the indicative 'is'. One can call this

Commented [GM10]: The way I read it, they don't explicitly set it at 18,000. In fact, they use case studies with a 20,000 figure. Therefore, I suggested this change here.

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9 There are many definitions of money laundering, summarised by Busioc (2007) and Unger and Rawlings (2006). Although, in many studies it is not clear what definition is being used: mentioning a definition at the beginning does not guarantee that the authors adhere to it and will not implicitly broaden its circle.

10 The methodology employed was reviewed by an 'external reference group' that included Prof. Dr. Friedrich Schneider from Johannes Kepler University of Linz and Prof. Dr. Brigitte Unger from Utrecht University (UNODC, 2011, p. 2)

indicative bias: sliding from the subjunctive modus of ‘may’, ‘might’ and ‘could’ to the indicative modus of ‘it is’ (See Van Duyne, 1993; Van Duyne et al., 2005).

Such an indicative bias can also be observed in the report of ECOLEF, drafted by the Utrecht School of Economics in which the phrase ‘available for laundering’ also plays an important role. ‘Available’ crime-monies are presented as a percentage of the GDP, which looks almost real. In the end the ‘results’ are ranked according to an “actualised %” of laundering threats (= ‘available’), though we are still within a hypothetical model which remains based on a defective definition and shady estimations as far as the alleged proceeds are concerned. Within the proposed models it looks convincing but as soon as one looks for independent empirical evidence, the model coverage becomes shallow and incoherent.

Outside the consensus models

There is more between heaven and earth than consensus models. What matters in the end is that the outcomes of a model are tested against ‘data on the ground’: assumption against refutation. To this end Ferwerda (2013) has listed the presumed effects of money laundering on the economy, of which he found 25 in the literature (the ‘consensus’), and tried to find empirical evidence for each of them. Using a large variety of (open) sources, the author had to admit that for most effects independent evidence was lacking, an observation that had also been provided by Reuter (2013). Worse, for many of the stated effects pretences of evidence had been made without any trace. Ferwerda quotes Barlett (2002) who stated: “It is clear from available evidence”, though without any reference to that alleged evidence. Nevertheless, Barlett, who discussed the effect of laundering on distortion of consumption, investment, savings, imports and exports, income and employment, demand for money, interest and exchange rates, corruption, reputation and increase in crime, got away with this unsubstantiated statement and was (and still is) widely quoted.

Concerning the almost ‘self-evident’ effect, the furthering of crime because of laundering, Ferwerda observed a measurement problem: laundering as a criminal act is counted in addition to the predicate offence. That entails that the independent variable of ‘laundering’ is also counted in the dependent variable ‘prevalence of crime’, making nonsense of the whole measurement exercise. More than a decade earlier Reuter and Greenfield (2001) came to the same conclusion. It is clear that it is time to move away from this large figure circus and its attendant over-reliance on numbers that are *“scientifically doubtful”* (Schneider and Windischbauer, 2008. p. 117; see also Van Duyne and Miranda, 1999; Reuter and Truman, 2005; and Reuter and Greenfield, 2001).

Alldridge (2003), citing van Duyne (1998), observes that if the amounts of crime-money had been near the sums estimated, the impact would surely have been noticeable, which it is not. We do not conclude that the inflow of crime-money in

certain markets, such as the real estate market, has not had any effect. There is recurrent 'anecdotal evidence' (widely spread over time and space) that crime-money investment in real estate had inflationary effects (Morocco: De Mas, 2001; Colombia: Keh, 1996). However, in what way do the effects of these crime-money flows differ from other money flows, e.g. originating from migrant labour savings or financial windfalls from the oil or minerals extraction industry (Van Duyne and Levi, 2005)? If badly managed oil money leads just as much to an unbalanced economy as the in- and outflow of crime-money, other and more relevant questions have to be raised.

For our objective to give meaning to the 'proportionality balance', the outcomes of this surveillance look bleak. The evidence scale of the threat balance is 'loaded' with unspecified concepts, assumptions underlying models which 'might' be true but which are nevertheless presented in the indicative modus of 'is'.

This is a dilemma: despite this empirical fuzziness we cannot dispense with the concept of proportionality, but we cannot make it sharper either. Perhaps we should leave the scale of threat and the evading evidence as it is − 'within brackets' − and accept that for most policy makers and their constituencies the mere semblance of evidence is already sufficient as justification for what they are willing to put on the other scale: the accumulated efforts of the fight against money laundering.

c. The effort side

Leaving the threat scale for a while 'within brackets' does not imply that the proportionality principle is no longer relevant. As a matter of fact it emerges all the time and in every measure that is taken to counter the threat of laundering: after all, these efforts are also presented as being in balance to the 'threat' whatever its lack of precision. Nevertheless, it is equally difficult to draw up an exhaustive list of measures and convert these into something measurable such as money spent in fighting money laundering. So we will look at the bits and pieces that are available. To that end we turned to the reported efforts of the FATF and its sister organisations and to their documents of such effort: the Mutual Evaluation Reports (MERs). From there we turned to the regulated sectors to find out whether there are reliable data about their efforts.

1. Mutual evaluations: much effort and little coherence

Since its establishment in 1989, the FATF has regularly issued 'Recommendations' to the national authorities to act against money laundering. The aim of the FATF is to have these Recommendations translated into legal and regulatory frameworks and implemented across the globe. In order to prevent a noncommittal attitude, this has to be supervised. One can say this constitutes a top-down effort in which the

FATF and its 'sisters', the FATF Style Regional Bodies (FSRBs), play a prominent role.[11] How is this role fulfilled and how much effort does it demand?

The FATF proclaims its objective as being to set standards and promote an effective implementation of measures against laundering.[12] That does not go for free. As the FATF is in essence a "policy making body"[13] and (in theory) not a kind of global inspectorate, it has no budget for supervising the implementation of its own Recommendations. This task is ceded to the Member States to evaluate their own money laundering policy against the 40 Recommendations plus special Terrorist Financing Recommendations (as modified from 1990, 1996, 2003 and 2012), using for each Recommendation a simple four point 'measuring rod', running from non-compliance to full compliance, which are summed to a final score. The stated purpose is to evaluate whether members have 'effectively' built up their controls and systems to prevent criminal abuse of the financial system.

Simple enough, but each review is expensive to execute, involving a team of four to six 'experts' with legal, financial and law enforcement expertise and two members of the FATF/FSRB Secretariat, IMF or World Bank, protracted visits, meetings and copious reports taking up to a year to complete with follow up responses from the reviewed nation occurring over several years. See Table 1.

Table 1 Summary of the Mutual Evaluation Report Process

Purpose of MER	Assessment of formal compliance with Recommendations and assessment of effectiveness of implementation. Rating for each Recommendation as Compliant (C); Largely Compliance (LC); Partially Compliant (PC); and Non-Compliant (NC); Not Applicable (NA).
Assessment team	Appointed by FATF Secretariat from FATF members, associate members, FATF-style regional bodies or international organisations with observer status.
Skills	The team will include experts in law, law enforcement and financial regulation with expertise in AML/CFT and includes a member of FATF secretariat. They will not necessarily have country specific knowledge
Scope of review	Institutional framework; AML/CFT laws, regulations and guidance including both law and regulatory enforcement; assessment of effectiveness of the system to deter ML and CFT
Documentation	FATF Methodology for Assessing Compliance with the FATF 40+9 and a Handbook for Countries and Assessors.
Approach	Pre-visit completion of a questionnaire, team visit for a period of 1-2 weeks comprising meetings with government officials and with private sector; post visit drafting of the report in consultation with officials within the country. The report is

[11] The FSRBs are: Asia/Pacific Group on Money Laundering (APG); Caribbean Financial Action Task Force (CFATF); Eurasian Group (EAG); Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG); FATF Latin America (GAFILAT); GIABA; Middle East and North Africa FATF (MENAFATF); Council of Europe (Moneyval).

[12] FATF website http://www.fatf-gafi.org/about/ (accessed 24/9/2015).

[13] FATF website http://www.fatf-gafi.org/about/ (accessed 24/9/2015).

	tabled at and further discussed at one of the Plenary meetings when the ratings can be amended and once consensus is reached the report is published. Within 2 years the inspected country has to report back to the plenary on progress made in addressing identified deficiencies.

Source: Adapted from Chaikin, 2009 pp 242-244, see also Levi and Gilmore (2002, p 346), Halliday, Levi and Reuter (2014, p 27).

This mechanism of mutual evaluation results in the production of as many MERs as there are Member States. It focuses on outputs (in particular STRs/SARs[14], convictions and asset recovery) and ignores the costs associated with any system (Chaikin, 2009, pp. 242-244; Sharman 2008, p. 641). The third evaluation round is just now drawing to a close and the fourth evaluation round has already commenced.

There has been little critical interrogation of this expensive area of the AML framework that sees a 'one size fits all' approach across multiple countries of different size, levels of development and thus relative financial sophistication. We find the absurdity of Vanuatu (266,937 souls) drafting its AML legislation as "a word for word copy of the UN model" right down to provision for non-existent complex financial derivatives (Sharman, 2008, p. 642). It looks like an example of what Van Duyne (2009, p.1) calls: a *"compulsive excessive regulatory disorder"*. It is also instructive that Levi and Gilmore (2002) pointed to the differential application in standards whereby the rules and sanctions are enforced more firmly against smaller states than against the USA.

We found three prior studies that have looked at compliance with individual Recommendations (attributing a numerical score to the compliance ratings) extracting information from individual country MERs, each of which has focused on a sample of countries. Arnone and Padoan (2008) and Johnson (2008), independently looked at the degree of compliance by Recommendation for samples of 20 and 16 countries using a four point constant interval linear scale. Ferwerda (2009) took another approach. Arguing that the assessment of the degree of compliance was influenced by the resources available to the country being assessed (with more expected of more developed countries), he proposed an alternative scoring system ranged across a 5 point scale that he applied to a sample of 17 countries. However, as there was no independent verification of his scoring, it too is open to criticism. Johnson (2008) looked at average levels of compliance before (from the self-assessment approach) and after 2003 (third round mutual evaluation) and concluded that there was a reduction in levels of compliance. However, as different groups undertook the different evaluations this remains interpretation rather than findings. One consistent observation from these studies was that there

[14] Suspicious transaction reports/Suspicious activity reports.

was overarching criticism of the MER reports with inconsistency in layout, in underlying quality and in overall size (Arnone and Padoan, 2008; Ferwerda, 2009; Halliday, Levi and Reuter, 2014).

We decided to take more detailed stock of the outcomes of the third evaluation round by selecting a large sample (about 90 reports) in the hope of being able to gain a better view on the effort side. To our knowledge no other studies have attempted to analyse such a large sample.

MERs are not for the faint hearted: the quality and readability varies widely. As noted in Table 1, the mutual evaluation is not a free exercise: after thorough preparation the targeted country is visited for an on-site inspection of about ten days by between four and 11 evaluators (average six) who issue a report of up to 650 pages (average 222 pages) in length. From the 90 reports that we reviewed there was much variation and little consistency. So, for example, Uganda (rated by Transparency International a lowly 2.7 corruption TI-index[15]) was reviewed in June 2005 under the auspices of the ESAAMLG[16] by a team of four evaluators. Their deliberations resulted in a slim volume of 82 pages despite the fact the average compliance rating (against the Recommendations) was 1.2 and modal compliance rating merely 1. Contrast this with France: (with a general corruption rating of 7.4 by TI), reviewed in February 2011 under the watchful gaze of the FATF by seven evaluators. They proudly produced a veritable tome of some 664 pages even though their modal and average compliance judgements were 3 and 2.9 respectively. Smaller jurisdictions with a relatively low crime rate, e.g. Denmark, or small financial markets such as Moldova (299 pages and seven evaluators) or geographically remote such as Vanuatu (four staff spending 12 days) appear to require as much or more energy of the evaluators than larger countries. All this is a major effort in terms of travelling and staff and has been estimated to cost some US$300,000 per evaluation (Halliday, Levi and Reuter, 2014, p. 49). Looking at it from the perspective of proportionality it was often 'much ado about nothing' and certainly not about a money laundering threat.

The subjective nature of assessment has resulted in the evaluation of compliance with recommendation rules (inputs). Even this cannot be measured consistently. No matter the number of times it is used, referred to and apparently 'measured', one review team's conclusion about what ~~is~~ effective compliance can be ~~and~~ is very different from that of another. This implies that the phrase 'partially compliant' can embrace such a range of responses it almost requires its own mini-calibration. Similarly, many of the reports assess 'compliant' simply on the basis of

[15] TI refers to Transparency International Corruption Perceptions Index. Although not a measure of money laundering, this is mentioned in the reports and is used here as an external indication of the potential susceptibility to laundering. The values reported are for 2005 and 2006, the start of the third round of evaluations.

[16] ESAAMLG: Eastern and Southern Africa Anti-Money Laundering Group.

control being present: box ticking wise. Effectiveness (outputs) seemed to be of subordinate concern. Incidentally the evaluators deplore the leniency of the (Scandinavian) courts and urge for a more repressive policy, apparently not realising that in democratic constitutions judges are independent. Consistent with the surreal comedy that was the trade-mark of the Monty Pythons Flying Circus television show, we observe comments such as this from the Danish MER: "The criminalization of the financing of terrorism by Denmark is fully compliant, but Greenland and the Faroe Islands have not yet adequately criminalized the financing of terrorism, terrorists and terrorist organizations." (Special Recommendation II p. 58[17]) So the rating is reduced to 'Partly Compliant' irrespective of the extremely limited potential for criminal or terrorist infiltration of the small economies of either Greenland (population 56,000) or of the Faroes (population 49,000).[18]

The effort in time and money does not end with the drawing up of the MERs. This tabular representation of the MER formula shown in Table 1 implies a closed end process that is complete at least within two years of the report being accepted. As discussed below, this is in fact far from the end of the matter as for many jurisdictions the resulting follow-up can go on for many years. All reports must be reviewed by two or more reviewers after which (with comments and annotations of the evaluated country) it is presented to the FATF for the next Plenary Session or at the Plenary of one of the FATF regional-style bodies. This is (frequently) a place of 'shame and blame'. Countries with flaws in their system or its implementation get 'homework' and have to submit follow-up reports till the Plenary is satisfied and the country can be relieved of its reporting duties. Countries that persistently fall short are subject to a visit by a 'High Level Mission' (a kind of severe FATF Headmaster) effectively demanding compliance.

Dependent on the approach of the FATF-style regional organisation, monitoring and follow up homework continues more or less frequently bearing little relation to the size of country, complexity of financial sector, apparent vulnerability to criminal infiltration or indeed original evaluation. We looked into the follow up procedure (or its absence) for a selection of countries. From this it can be observed that the Caribbean FATF (CFATF) is the most assiduous in the post evaluation follow up requirements that are placed upon individual countries. The CFATF requires twice yearly reports of many Member States. But the CFATF also took the decision at its El Salvador Plenary in May 2015 that all Members who had not exited the third round follow up process should simply be allowed do so by

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[17] MER available at http://www.fatf-afi.org/media/fatf/documents/reports/mer/MER%20Denmark%20full.pdf (accessed 25/9/2015).

[18] Denmark which, according to the ECOLEF report (p. 281) has the lowest 'threat level', is nevertheless reproached by the FATF for not having criminalised self-laundering.

November 2015. For other countries reviewed under the auspices of Asian/Pacific Group (APG) nothing further appears to have been warranted or if it was, it is not then publically disclosed. MONEYVAL appear to execute the most thorough of procedures including re-visits and reassessments by the 'high level mission' leading to further long reports.

Countries persisting in their unrepentant non-compliance may in the end be 'put into the corner' as a 'high risk and non-cooperative jurisdiction'.[19] This is not an inconsequential qualification: financial institutions transacting with these countries without enhanced due diligence may be sanctioned. Threat of international blacklisting (a now discontinued term) as sanction, refutes the idea of 'soft law' (Stessens, 2000). It is a verdict without appeal and as such it is debatable whether these aspects of the work of the FATF heed the principle of proportionality.

2. Proportionality and the Flying Circus of observers

In addition, we looked at the expense side of the social efforts of the FATF. The procedure of mutual evaluation is not the only 'tool' to maintain some kind of global socio-political coherence. Visiting each other, not only to conduct (and observe) MERs but also attending (as member and observer) the various (frequent) regional plenary sessions, training and updating workshop sessions or typology workshops is an ongoing social activity. The intensity of these social activities is not to be underestimated: it is not only a matter of one FATF, but of a further eight FATF Style Regional Bodies (FSRBs). The FATF itself currently comprises 34 member jurisdictions and 2 regional organisations. The eight regional 'FATF-ies' are its associate members, while there are observers from about 30 organisations represented in the plenary FATF meetings or other events such as typology workshops.

The phenomenon of observership is difficult to assess, but should not be underestimated, particularly not because of its quantity. There are some 93 institutions visiting the organisational events of both the FATF and FSRBs as observers. Three FSRBs have even more observers than Member States. The FATF, the IMF, World Bank, Interpol and the United States have observer status in five or more FSRBs. To this should be added the Egmont Group of Financial Intelligence Units of 151 member FIUs, of which the events are (potentially) attended by 19 observers, comprising mainly a selection from the 93 observing institutions. As these are global social relationships which imply a lot of travelling, one can imagine that the maintenance of bonds between so many sister

[19] The relevant countries are: Iran, North Korea, Algeria and Myanmar. The latter two have taken steps towards improving their AML/CTF regimes, but the FATF Plenary thinks it insufficient, particularly where it concerns terrorist financing. FATF Public Statement - 26 June 2015.

organisations and visiting observing relatives entails quite an expensive Flying Circus.

We are not the first to ask about the cost of this circus. Harvey (2011) drew a spectacular blank in her attempts to access budgetary information from the FATF and FSRBs; despite e-mail requests no information was provided. A similar blank wall was presented to our more recent enquiries (2015). Only three FSRBs presented any type of financial statement in their annual report and only the Asia and Pacific Group (APG) provided a breakdown of the annual budget of $ 3.2 million for the fiscal year 2014-15 of which $640,144 is to cover travel expenses for their Executive Secretary and 13 staff. The FATF itself has a budget line for travelling of almost $ 300,000. Similar budgetary information from other FSRBs or countries is not available. Nevertheless, even if it is not the case that "all visit all", it is plausible to assume some sort of a multiplier for the sum of these socio-institutional costs.

Commented [GM12]: Should we put 'US' here and elsewhere where we mention the dollar sign?
changed

3. Costs: budgets and staff

The MERs also provide us with some information about efforts in terms of staffing and budgets of a large number of the FIUs within our sample: in 32 cases a budget was mentioned. These data must be treated with utmost caution: not only because they can be outdated, but also because their meaning can be ambiguous unless the law enforcement backgrounds are taken into account. For example, Russia and Lithuania have FIUs with respectively 550 and 450 employees while the size of their economies obviously varies enormously. However, according to the report on Lithuania, "the AML regime is mostly used for the detection of other crimes" which the evaluators criticise as "unacceptable", though without explaining what is wrong with such a use.[20] The massive effort of Russia is rather to be compared with that of the USA FIU, which has a staff of 522 (2006) of which 107 are analysts. Whether these can be directly compared is problematic: the USA, having a bigger economy, a larger population and a longer AML-tradition, produced 1,075 money laundering convictions in the reporting year (not including convictions at state level) against 118 in Russia in the same year. The latter concern both 'stand alone' (25) and 'self-laundering' (93) convictions. There were 532 convictions with money laundering as "aggravating circumstances". A separate table "Cases containing FIU material" mentioned 95 convictions as FIU related.[21] This is the only clear reference to a connection between law enforcement output and FIU efforts.

Otherwise it is difficult to interpret the expenses/effort data of the MERs meaningfully without knowing the individual setting of the FIUs. For example the

[20] This provides an example of the 'meddlesomeness' of the FATF: financial investigation should serve to counter money laundering as well as crime-for-profit.

[21] MER Russia, pp. 39 and 61.

FIUs in Germany (2010, budget unknown) and Thailand (2007, budget $ 4,100,000) have 245 employees each, but Germany produced 766 prosecutions and 608 convictions against 12 prosecutions and no convictions in Thailand. One may wonder how effective the Thai effort is, compared to that of Germany. However, in Germany the number of staff only concerns the FIUs at state (Länder) level, while at the central (BKA) level, FIU functions are embedded in a special section on Joint Financial Investigation.[22] Indeed, comparing FIUs, whether using effort (input in staff, budget) or output numbers (prosecutions or convictions) is fraught with caveats. For example, the FIU of China has 80 staff and that of Romania 90 staff. However, there are regionally about 300 full time employees of the Peoples' Bank of China and a further 7,000 part-time, who perform FIU functions. Despite this difference, the outcome in terms of conviction is the same: one conviction for money laundering in each country (2006).[23]

The MERs do not comment on the apparent or perceived reputation of individual countries. However, we were surprised that the numbers appeared at odds with the 'reputation' of a country, e.g. its significance as a financial centre, without the evaluators taking this into consideration. For example, the British Virgin Islands is perceived as one of the 'hotspot' offshore centres (Van Koningsveld, 2015), together with the Cayman Islands or Luxembourg. So one might reasonably expect that this would be reflected in a substantial workload and corresponding size of the FIU staff. However, these three FIUs have a staff of six (BVI and Cayman Islands) or seven (Luxembourg) with an average modest workload input of 178 suspicious transaction reports and 6 convictions.[24] These FIUs are perhaps understandably small, given the size of the states, but one would expect some analysis of this matter in the MERs.

Commented [GM13]: But we must also think of the population of these islands. These are very small states with a limited workforce. Naturally, the FIUs will have small teams.

Overseeing our intermediary stock taking of the MERs from the perspective of efforts to be put into the scale to counterbalance the laundering threat, it looks like 'much ado about nothing'. When we go beyond the individual member state's efforts and include the efforts and connected expenses of the Flying Circus of the FATF and FSRBs and weigh this subsequently against the quality of the output, it is difficult to consider this as a display of efficiency. The readability of the reports is generally low and quantitative core information is often difficult to find efficiently. The redundancy is high and the internal coherence often low. We already commented on the difficulty of how the evaluators can give any rating of

[22] MER Germany, 2010, p. 112; MER Thailand, 2007; p. 85 and 97.

[23] MER Romania, 2008, p. 58; MER China, 2007. The Chinese statistics are somewhat non-transparent because 26 persons were convicted pursuant to art. 349 CC which covers hiding, transferring etc. narcotic drugs or their pecuniary gains which implies that both or only one condition needs to be fulfilled producing unreliable ML statistics.

[24] The authors of the ECOLEF report notice that Luxembourg (highest average income in the EU) was slightly more 'threatened' (according to the report) than other EU Member States.

efficiency and effectiveness of a country's performance in the absence of proper statistics. For example, the FIU in the Seychelles has no statistics but is found to be partially compliant. In this case the evaluators should have suspended their opinion, which did not happen. Another example is the phenomenon of corruption. In many reports ~~the TI~~ corruption ~~perceptions index~~ is mentioned as a problem, ~~but~~with the TI corruption perception index being specifically referred to, but without sufficient analysis of the government's and judiciary's ~~connection to the FIUs'~~ functioning ~~or~~ and of how corruption ties to ~~the~~ laundering ~~situation in general~~. For example, this concerns Russia, China, Bosnia and Herzegovina, and Greece. ~~no account was taken of the very negative corruption ratings for countries such as Russia, China, Greece or Bosnia Herzegovina. Likewise there is no mentioning of~~ More should have been said about bribe laundering as a reason to file a ~~n~~ STR to the FIU.[25] ~~But i~~If there is so much bribery, where are the related STRs? While the FATF meddles with the criminalisation of self-laundering (usually minor cases), we find no sign of FATF's concern for the absence of meaningful FIU statistics on bribe laundering ~~in the FIU statistics~~.

Commented [GM14]: In many reports corruption is mentioned as a problem, with the TI corruption perceptions index being specifically referred to, but without sufficient analysis of the government's and judiciary's functioning and of how corruption ties to laundering. For example, **this concerns Russia, China, Bosnia and Herzegovina, and Greece.** More should have been said about bribe laundering as a reason to file a STR to the FIU.[1] If there is so much bribery, where are the related STRs? While the FATF meddles with the criminalisation of self-laundering (usually minor cases), we find no sign of FATF's concern for the absence of meaningful FIU statistics on bribe laundering.

Concluding our search of the FATF efforts as something to put into the scale of the hypothetical proportionality balance, we find mainly a lot of fuzziness going together with a continuous deployment of much energy and expenses, but we find many indications that much of that energy is just dissipated.

4. Efforts related to the regulated sectors running the gauntlet between profit making and compliance

In order to better understand the proportionality of the AML regime and its effectiveness, the UK House of Lords held a hearing in 2008 which resulted in a two-volume report published in 2009. In its evidence to the same enquiry, the Law Society stated that

> "The mutual evaluations conducted by FATF do not consider the costs actually borne by the private sector in meeting their compliance obligations. The mutual evaluations also do not quantify the scale of the criminal economy in the relevant jurisdiction or the actual overall results in disturbing or preventing criminal activity achieved through the anti-money laundering regime in that jurisdiction".

The main costs are incurred by or on behalf of the regulated sectors. This is doubly plural: not only is the financial sector involved, but also designated non-financial businesses and professions (DNBPs). In addition, there are costs of supervision. Banks, credit institutions, stock brokers, casinos, but also lawyers, notaries, real estate brokers, car dealers, art dealers, auction houses and other traders in valuables

[25] The statistics of 'corruption mentioning' of these countries is also remarkable: Russia – 68; China – 27; Greece – 15 and Bosnia-Herzegovina – 73.

have to be supervised.[26] That does not go for free: supervising such an extensive and ramified field to check compliance of sometimes complicated 'Recommendations' (meaning 'demands') requires extra staff or a dilution of existing task performance. This creates 'resource tensions'. The ECOLEF Report (2013, p. 114) mentions various arrangements to spread the burden of AML/TF supervision across institutions.

This already indicates that this side of deployed efforts is difficult to assess as supervisory energy seeps at all sides through the regulated sector. The ECOLEF research team differentiate between five types of supervisory architecture:

- The FIU model: main agent and end responsibility;
- The external model: public administrative and government authorities;
- The internal model: own professional organs of supervision;
- The hybrid model I: a combination of internal and external authorities with end responsibility shared among the supervisors involved;
- The hybrid model II: responsibility shared between external, internal authorities and the FIU.

With the exception of the first modality, there are always more supervisory institutions involved as each distinct business area requires its own supervisor (for example one for the banks, one for the casinos, the notaries etc). In short, a lot of effort is deployed by numerous institutions to watch over compliance. How much does this cost? Unfortunately, when it comes to financial accountability hardly anybody can supply any breakdown except that AML/FT supervision alone is for most supervisors not a full-time ongoing task.

Apart from the expenses of the supervising institution(s) it is in the regulated sectors where the real work is carried out and where consequently most of the expenses are incurred. If we want to find data to answer our proportionality question we have to look at these multiple work floors of bankers, accountants, realtors and other entrepreneurs and professionals running the gauntlet between doing business and complying with recommendations: a 'minefield' for which they never asked (Gelemerova, 2009; Verhage, 2009b).

Unfortunately, no answers from these frontlines are forth coming. Focusing on the financial sector we find a combination of 'data opacity' and occasionally more detailed references to the costs of compliance. Costs data are fragmented across the various parts of the regulated sector and across jurisdictions with the implication that it is not known how much globally is spent on compliance. There have been attempts, particularly among the larger audit and risk management firms, to collect costs data. These firms have also undertaken surveys to identify trends and determine changes in costs. However, they face the challenge of banks that are not

[26] Together they form the category of Designated Non-financial Businesses and Professions (DNBP).

necessarily able and/or willing to provide specific details of AML related costs. It may be difficult to single out compliance costs because many reporting entities, particularly banks, execute their anti-fraud and AML activities within the same unit and by the same persons. This results in combined costs which are difficult to keep apart. There are also expenses which are also inherently difficult to capture such as the risk avoidance costs: declining to take a customer on board because the account manager notices something unusual, which may be a risk, or because this potential customer is outside the bank's desirable risk parameters, i.e. its 'risk appetite'. As banks are encouraged to operate 'risk based', it may be rational conduct on the side of account managers to avoid any risk which also implies lost opportunities to make money. To complicate things, there are also saved future compliance costs in this de-risking. Such cost factors are difficult to identify.

When clients are taken on board, there are a number of mandatory activities: due diligence (perhaps in an enhanced form) and reporting suspicious or (depending on the country) even unusual activities. Carrying out due diligence costs staff time, in particular in cases of a politically exposed person (PEP), but this can also be cost saving in cases where a risky client is turned down for valid reasons (one usually cannot fully know).

The costs that are easier to recognise and measure as compliance costs (in general as well as client specific) would include the following:

1. administrative costs at any stage of compliance, e.g. in relation to obtaining KYC documents);
2. legal costs, e.g. legal fees for the preparation of contract clauses relating to AML and related compliance, e.g. sanctions and anti-corruption assurance;
3. investment in technical products and software to assist compliance;
4. investment in staff: this includes salaries, training and conference attendance to be part of the community of stakeholders.

But with such a typology we still do not have a cost estimate, because that requires insight into the budgets allocated by financial (and other regulated) institutions to perform these tasks. Here we face a double impediment. Big financial institutions which have a separate compliance department are likely to have a specified budget which may reveal a part of the compliance costs, namely those within that budget unit. Compliance interwoven with other financial service activities will remain invisible. In addition, such budgets will usually not be made public or a clear breakdown will not be available, because it constitutes 'corporate sensitive information'.

Surveying the various reports on the costs of the AML regime, we first note that respondents from the financial industry could not be presented as suitable suppliers of costs data of their own branch. This is not only caused by the opaque situation mentioned above but also is due to unwillingness. Specific costs, such as staff

extension or buying new IT equipment must have a price tag. If not precise, then at least a 'ball park' indication. So the reports mention IT costs as a generally acknowledged 'main cost driver' but do not produce a market conforming estimate.

One of the earlier reports we inspected for data on compliance costs was commissioned by the municipal government for the City of London and carried out in 2005 by consultancy firm Z/Yen.[27] Apart from data from open sources, the findings in the report derive from interviews with 386 employees from the financial service sector of which 105 are from the international sector. The countries compared were: the UK and the US mainly with Germany, Italy and France occasionally added. When it comes to estimation, the unexplained "best estimates" pops up, which works as follows: if there is a range between two estimates, the next "best estimate" is then the midpoint between the extremes. Is that an average or a median? There is no mentioning of a supposed underlying frequency distribution. These estimates are nothing but expressed opinions. If we substitute the word 'estimate' for 'opinion', all statements about 'best estimates' become tautologies about 'best opinions'. It illustrates the extent to which we are deceived by a specific 'AML congregation' language. We remind the reader of what we remarked earlier about the 'indicative bias': slipping from 'may be' to 'is'.[28]

The New Zealand Ministry of Justice commissioned Deloitte to assess compliance costs of its AML requirements.[29] The report provides a detailed account per financial industry branch and denoted non-financial sectors of (a) start-up and (b) on-going (estimated) expenses. It remains fairly independent in judging the reasonableness of estimates as given by respondents, adding its own adjustments. Thus, the provided estimates of start-up costs and on-going costs of NZ $227.6 million and NZ $128.2 million per year were adjusted to what the rapporteurs thought more plausible: NZ $111.8 million and NZ $42.7 million per year respectively. Nevertheless, with only 32 interviewees spread over 15 targeted sectors the empirical basis is too small for further extrapolations.[30] Deloitte's observed need to moderate the claims of the interviewees, who may not have verified or validated their cost statements, points at serious caveats that form part of all these estimation surveys: interviewees are unreliable estimators if they must

[27] M. Yeandle, M. Mainelli, A. Berendt and B.Heal: Anti Laundering Requirements: costs, benefits and perception. City Research Series (no. 6).

[28] Other aspects not discussed here concern the severity of the anti-laundering measures, which were considered to be disproportional by the UK interviewees.

[29] New Zealand: Assessment of business compliance costs of the indicative anti-money laundering regulatory requirements. Ministry of Justice, July 2008.

[30] Deloitte gave a stiff disclaimer at the end of the introduction (p. 4) of which the last sentence read: "We provide no assurances that the cost estimates will remain relevant beyond the date of this report and accept no accountability or responsibility for any changes to these estimates which might be occasioned when the final anti money laundering regulatory requirements become available."

consult their memory. Still, they are treated like oracles. The lack of certainty appears to arise from the fact that clear figures (if available) are rarely disclosed.

A report by consultants of Europe Economics[31] in 2009, on behalf of the European Commission, aimed to study the effects of five measures of the Financial Services Action Plan, among them the third AML Directive.[32] For the study, 78 firms were interviewed from across the EU classified as: Banks and financial conglomerates; asset managers; investment banks and financial markets. Though the many tables suggest some exactness, nothing is further from the case. Again the 'best estimate methodology' is based on "quantifying the impact of the Directives into a series of steps and thought experiments . . . which we hoped to be, in large part, intuitive" (p. 124). Otherwise the whereabouts of the outcomes are a mystery "(since in many cases the numerators and denominators would not be exactly comparable" (p. 50). So we find tables with averages and medians without absolute clarity as to the total sample size or underlying frequency distributions. There is also a further big uncertainty: the absolute totals of the 2007 operating expenses, which is the ultimate denominator of the proportions of one-off and on-going costs of the separate measures. These are interview based without indication of other independent sources. Perhaps the report is the best 'intuitive thought experiment' we came across.

Commented [GM15]: In an earlier footnote we had the title in inverted commas and I made a comment about that.

KPMG – "named Global AML *firm of the year 2014*" − elaborated on the global costs of compliance.[33] The research tool consisted of a questionnaire to which 317 persons responded, all in knowledgeable positions within the financial industry spread worldwide. Among other things, they were asked to give an estimate of the increase in compliance costs: "How much has total investment in AML activity increased compared to three years ago?" This is a difficult question: it supposes knowledge of two points in time plus a judgment: knowledge of the present AML specific expenses and those three years earlier (which is the 100%) about which subsequently a comparative estimate must be made in percentages with broad and unequal ranges (p. 13: 25-50%; 50-100% and > 100% increase). No specific numbers are asked concerning identifiable compliance actions that are not interwoven with ongoing compliance activities ("sunk costs"): for example the acquisition of new monitoring tools or the outsourcing of certain tasks. These are distinctive costs which must be budgeted. If they cannot be disclosed because of being 'business sensitive', then that should have been mentioned as part of the methodological accountability.

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[31] Study on the Cost of Compliance with Selected FSAP Measures. Final report by Europe Economics. London, 5 January 2009.

[32] Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing.

[33] Global Anti-Money Laundering Survey. KPMG, 2014.

Surveying these findings from the regulated sectors, based on the above discussed reports, there is an objective and a subjective outcome. In objective terms there are no concrete data to determine the sum of the efforts as a proportionate counterbalance to alleged money laundering threats. Subjective data abound, mainly indicating that most interviewees think that the expenses of compliance are steadily increasing. But to what end and what are the objectives? There is no clear answer to this question except the answer which is most frequently mentioned in the literature: "to avoid being sanctioned by the supervisors", which is felt as the real threat. It is therefore good to close this section with a few opinions of interviewees on effectiveness worth quoting:

> "The current requirements are a completely disproportionate response to money laundering – there are far too many reports, far too much wasted time and far too much bureaucracy – and you can quote me on that!"
> A London based accountant (Y-Zen, p. 31)

This complaint does not stand alone: inefficient bureaucracy may go hand in hand with the institutional success of the global FATF-regime which may be taken for the ultimate aim. In response to this state of affairs the regulated industry responds with its own cost-effectiveness of doing the minimum:

> "The idea of customer identification is clearly sensible but the actual customer identification process that most banks employ is simply not effective – it is a box ticking exercise"
> MLRO at a UK-based retail bank (Y-Zen, p. 42).[34]

Conclusions and discussion

> *Customer: "Not much of a cheese shop really, is it?"*
> *Shopkeeper: "Finest in the district, sir."*
> *Customer: "And what leads you to that conclusion?"*
> *Shopkeeper: "Well, it's so clean."*
> *Customer: "It's certainly uncontaminated by cheese."*
> Monty Python's Flying Circus: the Cheese Shop[35]

In this chapter we addressed the global AML regime from the perspective of proportionality, a principle inherent in any justification of regulatory or criminal

[34] Similar quotations appearing in academic papers (Favarel-Garrigues, et al, 2011; Verhage, 2009; Harvey and Lau, 2009).

[35] Monty Python's Flying Circus ran on BBC TV from 1969 to 1974. This quotation is taken from: http://www.telegraph.co.uk/comedy/comedians/monty-python-s-25-funniest-quotes/ (accessed 2/10/2105).

law action. Despite its ubiquitousness it is a difficult concept to operationalise best captured by the metaphor of balance with a pair of scales. In our field one scale is to be 'filled' with the 'threat against' and the other scale with the 'weight of the state', a shorthand for all countermeasures. By their nature both are composites making operationalisation far from easy. Still, this principle remains indispensible and also in the field of money laundering the task of specifying what has to be placed in the two scales must be taken seriously: for each measure proposed, the proportionality question relating to the threat has to be addressed.

Our *tour d'horiz*on of what can be put into the scale at the 'threat side' proved to be disappointing in its yield. On the one hand we find a 'self-quotational' reality of a stakeholders trinity: the IMF/World Bank, the United Nations and the FATF, around which we find a host of interested beneficiaries: supporting economists, researchers and consultants confirming the 'consensus'. In Van Duyne (2011) this was qualified as a kind of congregation of believers. Within this congregation one meets a repeated depiction of serious money laundering threats as a justification for the 'heavy' global AML regime as it developed over the past four decades. However, as soon as one applies the basics of the empirical discipline, the underpinning of these threats prove to be quicksand: bad methodology with scattered islands of 'anecdotal evidence' preventing one from sinking away. The estimates are crude and reflect more belief than knowledge. For example, the proposed threshold of criminal income of € 18,000 above which laundering is assumed finds no support in the reality of criminal money management. Nevertheless, they are considered 'best estimates'.

Looking at the conceptual coherence we find an abundance of fuzziness. This concerns not only the core concept of laundering itself, but also the second most frequent concept suggesting an empirical meaning: 'available for laundering'. As far as the looming threat is concerned: it looks like a persistent bad-weather forecast of (financial) heavy weather but which in the past 25 years never came true. Looking at the proportionality balance we must conclude that there is not much that is solid to put into the 'threat scale'.

Subsequently we looked at the 'weight of the state': the sum of the (international) legal and institutional countermeasures. That is very wide and therefore we had to be selective in our approach. Because the MERs (efforts and contents) cover all recommended measures as well as some other costs aspects of the FATF and FSRBs, we studied a large sample of them.

The MERs testify an unparalleled institutional global success, irrespective of proportionality: no government or regulated sector can shirk the FATF authority. But given the stick of 'non-compliance' it can wield, one can no longer speak of informal power or 'soft law'. Likewise one should not take the word 'Recommendation' as implying something one may take into consideration. The IMF, lurking behind the FATF, is unambiguous about this: "For the purposes of

assessing compliance with the FATF Recommendations, the word should has the same meaning as must."[36] Woe betide the country which challenges this claim: it risks being put into the non-compliance corner.

But with that success come the expenses– ultimately passed onto ordinary customers (e.g. of banks) and taxpayers– and with that the connected proportionality question: does this whole regime counter the threat of laundering in a proportional way? First we have the extensive mutual evaluation circus which at the average costs *'in excess* of $ 300,000*'* (Halliday et al, 2014, p. 49) per turn does not go cheap. But do we have for this price a real 'quality instrument'? The findings of our survey as well as that of Halliday et al. (2014) point at a negative answer: despite its unwieldy volumes, the MERs lack in many regards coherence and are difficult to compare. Most evaluators use a box ticking methodology without questioning whether certain recommendations are of any relevance for the evaluated jurisdiction. Indeed, for a number of countries some recommendations may have come from another planet.

In addition, the whole bureaucracy surrounding the application of the MERs as well as the FATF and FSRBs should be questioned according to its proportionality. We observed a dense network of observers frequenting each other's Plenaries, workshops and seminars. Some FSRBs have even more observers than member states. The Monty Pythons Flying Circus may indeed be no exaggerated metaphor.

It is interesting to observe that another dimension creeps into the reports: maximum repression devoid of any tempering proportionality. Evaluators frequently criticise countries that have in general a lenient sentencing culture, as well as for laundering offences: no 'dissuasive punishments'. In their unbounded zeal the evaluators seem to forget that a basic constitutional principle of a democracy is the independence of the judiciary. Exerting pressure on lenient countries may be interpreted as an intrusion of sovereignty. The same applies to the phenomenon of 'self-laundering' on which evaluators (and the FATF) keep harping when they evaluate countries where, for carefully weighed reasons, (forms of) self-laundering are not criminalised, actually an option left open by the 1990 Council of Europe Convention.[37] Nevertheless, it is mentioned as a shortcoming. But how important is the phenomenon of self-laundering financially? Apparently important enough that encroaching on a countries' sovereignty is considered proportional to its 'threat'.

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[36] International Monetary Fund and the World Bank: Twelve-Month Pilot Program of Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) Assessments; p. 78.

[37] The 1990 Council of Europe Convention No 141 on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (the Convention, which became known as the Strasbourg Convention, was adopted in September 1990, opened for signing on 8 November the same year, and entered into force on 9 January 1993).

Subsequently we surveyed the evidence presented by the regulated sectors. Where the FATF, its sister organisations and all the ongoing supervision and maintenance of networks do not seem to reflect much proportionality in relation to the money laundering threat, for the regulated sectors the proportionality issue is different and much sharper. Here we find enterprises at the front line who are burdened with new tasks and extra expenses. They are distant from shadowy threats wrapped in evaporating macro estimates of biblical dimensions at IMF and FATF level. Their AML tasks in terms of the office equipment and staff costs must be directly proportional to the threat they tangibly experience. And what does this amount to? In the first place the supervisors' authority to sanction lack of compliance (Harvey and Lau, 2009; Levi and Maguire, 2004, Gelemerova, 2011); then, of course, risky persons who may harm the institution and finally their reputation. The reputational risk is perhaps most frequently mentioned in the many warnings of the national supervisors and authorities. However, to what extent is this again a product of the official prayer wheel? The history of 'secrecy havens' like Switzerland or Liechtenstein shows that savers do not run away from banks that launder, but rather from banks that lose their money (Harvey and Lau, 2009).

These considerations and statements from interviews indicate that at the work floor the experienced proportionality balance between threat and measures is different from the one conveyed at policy making and political level. This difference must be realised to prevent a top-down blaming of the work floor for all kinds of shortcomings. Before such brow-beating downwards, serious flaws should first be exposed at the level of the self-centred Flying Circus from which policies are imposed rife with fuzzy concepts and looming threat images that have not yet come true.

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