

## I. INTRODUCTION

1. The International Monetary and Financial Committee (IMFC), at its September 2000, meeting, requested “the Fund to prepare a joint paper with the Bank on their respective roles in combating money laundering and financial crime, and in protecting the international financial system.” Moreover, the two institutions were asked to explore incorporating work on financial system abuse, particularly with respect to international efforts to fight against money laundering into its various activities, as relevant and appropriate.

2. An informal question and answer session with the Fund Board was held in February 2001 on the basis of the staff paper *Financial System Abuse, Financial Crime and Money Laundering* □ *Background Paper* (SM/01/46); in September 2000, Bank staff prepared an information note for the Bank Board on *The Role of the World Bank Group in Promoting the Integrity of Financial Markets* (September 21, 2000). These documents provide relevant background material for this paper. A joint Fund/Bank workshop on financial abuse, with seven outside speakers (including the current President of the Financial Action Task Force (FATF)), was held at the Fund on February 27, 2001.

3. Although no formal conclusions were drawn from these meetings, the following propositions seemed to gain some acceptance:

- (i) while financial abuse covers a variety of activities, it would be productive at the present time to concentrate on the role of the Fund and Bank in efforts to combat money laundering;
- (ii) the Fund and the Bank are already helping countries strengthen their financial supervision and regulation, as well as legal and governance structures, contributing to the prevention of financial sector crime and money laundering;
- (iii) substantial efforts relevant to countering money laundering are undertaken by other bodies and closer international cooperation would benefit all; and
- (iv) the Fund’s and the Bank’s work on strengthening financial supervision through the application of financial standards, including the preparation of relevant Report on the Observance of Standards and Codes (ROSC), overlaps with the financial/supervisory aspects of the Financial Action Task Force 40 Recommendations (FATF 40).

4. This paper proposes that the Fund and the Bank strengthen their role in the global fight against financial sector abuse, and money laundering specifically, by (i) publicizing, through official statements and other forms of outreach, both the need to put in place the necessary economic, financial, and legal systems designed to protect against money laundering and the role that the Bank and the Fund are playing in helping to meet this need; (ii) recognizing the FATF 40 as a standard for anti-money laundering useful for Fund/Bank operational work, (iii) when undertaking Financial Sector Assessment Program (FSAP), ROSCs and Offshore Financial Center (OFC) assessments, intensifying the focus on anti-

money laundering elements in the assessment of supervisory standards□Basel Committee Principles (BCPs), International Organization of Securities Commissions' Objectives and Principles for Securities Regulation (IOSCO Principles), and the International Association of Insurance Supervisors Insurance Supervisory Principles (IAIS Principles)□and producing a detailed assessment which, with the concerned country's permission, could be published or shared with the FATF and/or the appropriate regional anti-money laundering task forces; (iv) working more closely with the major international anti-money laundering groups; and (v) increasing the provision of technical assistance (TA) from the Bank and Fund in this area.

5. Section II discusses work currently undertaken by the Fund and Bank that is relevant to countering financial abuse, especially with respect to helping national authorities improve their systems of financial regulation and supervision so as to create the environment within financial institutions to deter financial crime and money laundering. The paper then reports in Section III on the wider international efforts, including the work of the FATF and regional anti-money laundering task forces, in combating money laundering. Steps to enhance the Fund and Bank contributions to anti-money laundering efforts are proposed in Section IV. Section V discusses the resource implications. The key questions before Executive Directors (Section VI) are (a) whether the FATF 40 should be recognized as a standard for Fund and Bank operational work; and (b) how to enhance work on money laundering issues in Fund and Bank activities, in particular in technical assistance, including with respect to FSAP, ROSCs and OFC assessments, as well as in the context of technical assistance.

## **II. THE FUND'S AND THE BANK'S ACTIVITIES RELEVANT TO THE COUNTERING OF FINANCIAL SYSTEM ABUSE**

6. Money laundering is a problem of global concern, requiring concerted and cooperative action on the part of a broad range of institutions. The Fund and the Bank's principal contributions to the fight against money laundering have been in their work to promote stronger financial, economic, and legal systems in general. Strengthened supervisory systems and robust legal and institutional framework for financial institutions help prevent a broad range of financial sector abuses, including money laundering. This section first discusses the activities special to each institution, then turns to those pursued jointly.

### **A. Fund Activities**

7. Financial sector issues are central to the Fund's mandate as they are rooted in its purpose to promote macroeconomic stability and growth.<sup>1</sup> Anti-money laundering issues related to financial supervision and regulation (primarily those included in BCPs, IOSCO or IAIS Principles) are germane to the Fund's core responsibilities, while other anti-money

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<sup>1</sup>In April 1997, at the conclusion of the Biennial Review of Fund Surveillance, the Board called for increased attention in the period ahead to capital account and financial sector and banking sector issues (SUR/97/38, April 3, 1997). At the conclusion of the 2000 Biennial Surveillance Review, Directors recognized financial sector issues as one of the core issues in Fund surveillance (SUR/00/32, March 21, 2000).

laundering issues associated with criminal law enforcement (primarily those not included in BCPs, IOSCO or IAIS Principles) are beyond the Fund's core areas. Under existing Fund policies, anti-money laundering issues other than those relating to financial sector regulation and supervision are covered under surveillance and conditionality, as with other governance matters,<sup>2</sup> only if they pass the macro-relevance test.<sup>3</sup> The Fund could raise the issue of cross-border implications of money laundering, e.g., during the Article IV consultation, for a given member when this is macro-relevant for other members or important for stability of the international financial system (under Article XII, Section 8).

8. The Fund in its broad operational activities—surveillance, conditionality and technical assistance—promotes stronger financial systems, including through FSAPs, OFC assessments, and ROSC exercises. The Fund's work helps national authorities strengthen their supervisory and regulatory systems which, in turn, helps both to promote the safety and soundness of the financial sector and to create an environment that prevents financial system abuse. In particular, assessments of observance of international standards, codes, and best practices in the areas of financial supervision, prudential regulation, transparency of fiscal and monetary policies, and data provision and dissemination have the potential to play a major role in fostering financial market integrity. In this context, the Fund staff has followed the guidance given in *Concluding Remarks Following the Executive Board Discussion of the Fund's Role in OFC Assessments (Offshore Financial Centers—The Role of the Fund)* (BUFF/00/98), July 14, 2000). Directors stressed that effective anti-money laundering measures were important for the integrity of the financial system as well as for fighting financial crime, and that such measures were part of the core supervisory principles covering all financial sectors. Directors also noted, however, that anti-money laundering measures promoted by FATF included law enforcement measures, which would not be appropriate for the Fund to assess.

### **Surveillance and conditionality**

9. The emphasis on financial sector soundness in Article IV surveillance has increased in recent years.<sup>4</sup> In an earlier review **of the coverage of financial sector issues in**

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<sup>2</sup> See *Summing Up by the Acting Chairman of the Review of the Fund's Experience in Governance Issues*, Executive Board Meeting 01/14, February 14, 2001, (BUFF/01/22, February 22, 2001). The 1997 Guidance Note on Governance stressed a more comprehensive treatment of governance issues within the IMF's mandate and expertise. The note recommends, *inter alia*, a more comprehensive treatment in the context of both Article IV consultations and IMF-supported programs of those governance issues that are within the IMF's mandate and expertise.

<sup>3</sup> While the empirical evidence on the magnitude of financial system abuse including money laundering is limited, significant macroeconomic effects on individual countries cannot be ruled out.

<sup>4</sup> See *Summing Up by the Acting Chairman, Biennial Review of the Implementation of the Fund's Surveillance and of the 1977 Surveillance Review*, (SUR/00/32, March 21, 2000).

**Article IV surveillance**, staff found that assessments of banking systems and prudential and supervisory frameworks were discussed in almost every report reviewed.<sup>5</sup> As a follow-up and in order to provide a snapshot of the treatment of financial system abuse issues, a sample of staff reports in the context of Article IV consultations and use of Fund resources was reviewed for references to financial system abuse issues. Taking into account that explicit operational guidance to staff on the Fund's role in addressing anti-money laundering issues is both limited and recent, the sample focused on staff reports for members hosting major financial centers and those members included in the lists published by the Financial Stability Forum (FSF), FATF, and OECD.<sup>6</sup> Accordingly, the staff survey covered 48 staff reports issued during January 1999–December 2000.<sup>7</sup> Staff reports were examined for the coverage of money laundering, other financial crime (e.g., pyramid schemes, fraudulent sale of financial instruments), tax evasion, and corruption related to the financial sector. The reports were also reviewed for coverage of banking secrecy, which may contribute to financial abuse, as well as of the offshore financial activities that may be subject to less stringent regulation and supervision and thus potentially susceptible to financial system abuse.

10. **More than half of the staff reports reviewed included references to financial system abuse-related issues.** Specifically, 19 reports covered money laundering, six referred to financial crime generally, eight to banking secrecy, 12 to tax avoidance (or tax havens), and six to corruption. Six staff reports included specific references to the authorities' reaction to their countries being placed on one of the lists promulgated by the FSF, FATF or OECD alleging substandard compliance with their particular criteria.

### **Technical assistance**

11. Staff has provided **technical assistance on the design of prudential regulation and banking supervision schemes of many Fund members.**<sup>8</sup> The most extensive TA in this

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<sup>5</sup> Sixty-six Article IV consultation reports for emerging market and transition economies in 1998 and 1999 were reviewed. See *Biennial Review of the Implementation of the Fund's Surveillance and of the 1977 Surveillance Decision*, (SM/00/40, February 18, 2000), pages 23-26.

<sup>6</sup>Major financial centers include Germany, Hong Kong SAR, Japan, Luxembourg, Singapore, Switzerland, United Kingdom, United States. Others countries include Antigua and Barbuda, Bahamas, Bahrain, Barbados, Belize, Costa Rica, Cyprus, Dominica, Grenada, Israel, Lebanon, Liberia, Malaysia (Labuan), Maldives, Malta, Mauritius, Panama, the Philippines, Russia, Seychelles, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Tonga, and Vanuatu.

<sup>7</sup>The sample includes 3 use of Fund resources reports, 2 combined Article IV and use of Fund resources reports and 43 Article IV reports.

<sup>8</sup> Technical assistance reports by MAE during January 1992–October 2000 were surveyed for references to money laundering. Of a total of 998 MAE technical assistance reports electronically available, 115 reports contained references to money laundering.

area has been provided in the context of OFCs, FSAP, and ROSC modules.<sup>9</sup> **The OFC assessment program** has involved missions to 17 jurisdictions between October 2000 and March 2001. A progress report on the program was provided to the Fund Board on February 9, 2001. Anti-money laundering legislation, regulations and practices are being put in place by a number of jurisdictions, some with the support of Fund TA. Many of these OFC jurisdictions intend to request a Fund assisted assessment of financial sector standards and codes or an FSAP-type comprehensive assessment of their financial systems. FSAPs and ROSCs involve both the Fund and the Bank, and are discussed below.<sup>10</sup>

## **B. Bank Activities**

12. Consistent with its development mandate and comparative strengths, the Bank Group has been contributing to the global efforts to combat financial abuse and money laundering in three ways:

- First, helping countries identify and address structural and institutional weaknesses that may contribute to the lack of market integrity and potential for financial abuse.
- Second, participating in targeted international efforts to combat money laundering based on its mandate and expertise.
- Third, ensuring that the Bank Group's own financial transactions do not inadvertently undermine international actions to curb illegal practices.

### **Strengthening structural and institutional underpinnings**

13. As a global development institution, helping countries put in place strong economic, financial and legal foundations is the principal contribution that the Bank can make to the efforts to combat financial abuse. In recent years, the Bank has stepped up these efforts and is taking a more systematic approach in partnership with others, especially the Fund. There are three main related areas of work that are of particular relevance to increasing resilience against financial abuse, and where the Bank has deepened its involvement:

14. **Anti-corruption, governance and public financial management.** The Bank has greatly expanded its program in the areas of anticorruption, governance and public financial

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<sup>9</sup> This work has been discussed by the Executive Board. See, for example, *Offshore Financial Centers—The Role of the Fund* (SM/00/136 and BUFF/00/98), *Financial Sector Assessment Program—A Review—Lessons from the Pilot and Issues Going Forward* (SM/00/263, November 27, 2000 BUFF/00/190, December 12, 2000), and *Experience with Basel Core Principles Assessments* (SM/00/77).

<sup>10</sup> Currently, assessment of BCPs are defined as being within the Fund's direct operational focus (Group 1). IOSCO and IAIS Principles are defined as being within both the Fund and Bank's operations focuses (Group 2). All three are generally assessed under the FSAP, and separate ROSC modules on these standards have increasingly been prepared as part of the FSAPs. See *Assessing the Implementation of Standards—A Review of Experience and Next Steps* (SM/10/11, January 12, 2001).

management.<sup>11</sup> Since the launch of the Anti-Corruption program in 1997, the Bank has supported more than 600 lending and non-lending activities in approximately 90 countries aimed at stimulating institutional reforms needed to reduce corruption and strengthen governance. These include, for example, adaptable program loans and technical assistance operations designed to enhance capacity and reform incentives in the civil service (including for employees of public financial regulatory bodies); reforms in the financial sector, in public financial management systems, and in tax and customs administration; and programmatic adjustment loans that focus on improving accountability and transparency in the public sector through strengthened legal, regulatory and judicial systems and reforms in expenditure management and financial accountability. Economic and Sector Work (ESW) to deepen understanding of the sources and mechanisms of corruption and other types of institutional dysfunction has expanded markedly, with increased use of diagnostic instruments and surveys and the new Institutional and Governance Review. CAS task managers are now required to take corruption into account when formulating country programs and designing individual lending operations, and each CAS is reviewed for its realism in dealing with in-country governance issues. There has been a marked increase in the amount of analytical work done on public expenditure and financial management systems, increasingly in partnership with borrowers and donors. Stronger control and governance of public finances, in particular, are seen as essential foundations for adjustment and programmatic lending across the board.

15. **Strengthening financial systems.** The Bank deploys a wide array of activities to help countries carry out financial sector reform, with focus primarily on longer-term development issues. Prior to the Asian crisis, financial sector lending (adjustment and investment loans as well as technical assistance) amounted to US\$2.2 billion per year on average, but financial sector lending increased dramatically in the aftermath of the recent financial crises, amounting to an average of US\$4 billion over the past three years. In the 1990s the focus has shifted to a wide range of structural and policy dimensions affecting the financial sector, including, inter alia, the legal, regulatory, and supervisory framework for the banking industry, the insurance sector, capital market development, payment and settlement systems and bank restructuring and privatization.<sup>12</sup> In the current fiscal year, the Bank's financial sector staff are also undertaking economic and sector work in more than 22 countries (in addition to the FSAPs), conducting policy analysis and research on cross-cutting financial sector policy issues, and implementing more than 130 technical assistance projects in nearly 50 countries and regions.

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<sup>11</sup> For more detailed information on the Bank's governance, anticorruption, and public sector reform programs, see *Helping Countries Combat Corruption: Progress in the Bank since 1997*, September 2000, and *Reforming Public Institutions and Strengthening Governance: A World Bank Strategy*, November 2000.

<sup>12</sup> See *Strategy for the Financial Sector: Draft Final Report (R2000-169)*, August 19, 2000, discussed by the World Bank's Board of Executive Directors on October 19, 2000.

16. **Market infrastructure and integrity.** Financial market integrity requires a well functioning legal framework and sound practices. The Bank has increased its efforts in several areas that are key to a robust market infrastructure, and that have been highlighted in the wake of recent financial instability. In particular, the Bank has stepped up its programs to strengthen legal and judicial reform and institutions, corporate governance, accounting and auditing and market transparency.<sup>13</sup> In this, the Bank has sought to develop its partnerships with other institutions to enhance leverage and reduce costs. For example, it has established the *Global Corporate Governance Forum* with the OECD which is aimed at promoting a broad based dialogue and at helping developing and transition economies strengthen their corporate governance regimes. Similarly, the Bank participates and plays a catalytic role in the *International Forum on Accountancy Development*, which is a broad based public-private partnership to support sound accounting and auditing practices at the global and country level.

### **Contribution to international efforts to combat money laundering**

17. The Bank has been contributing to international efforts targeted at money laundering more specifically in three ways: (a) by participating in international discussions (e.g., FSF, FATF, OECD Forum on Harmful Tax Competition); (b) focusing on financial abuse in the context of economic and sector work and policy dialogue, and now in a more focused way through the joint FSAP program; and (c) providing limited technical assistance to countries to strengthen anti-money laundering programs.<sup>14</sup>

18. The Bank has recently focused its efforts in small developing economies which are especially susceptible to potential financial abuse, including money laundering, and need support in putting in place the policy and institutional foundations and specific provisions that are needed to reduce the risks of such abuse. The recent Financial Sector Strategy Paper<sup>15</sup> affirms the Bank's commitment to helping small economies tackle the development challenges that may stem from international initiatives aimed at fighting money laundering.<sup>16</sup> As noted in the background document for last Fall's First Annual Small States Forum,<sup>17</sup>

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<sup>13</sup> For further details on the Bank's role in helping countries strengthen corporate governance and accounting and auditing, see *International Financial Architecture: An Update of Bank Activities*, September 13, 2000 (DC/2000-20) and *Assessing the Implementation of Standards: A Review of Experience and Next Steps*, The International Monetary Fund and the World Bank, March 2001.

<sup>14</sup> One such case is the Colombian Financial Market Development Project program which aims to establish a Financial Intelligence Unit that will collect, monitor and analyze relevant information on suspicious transactions from the financial and the private sectors.

<sup>15</sup> *Strategy for the Financial Sector: Draft Final Report* (R2000-169), August 19, 2000.

<sup>16</sup> Fourteen Bank's eligible countries are on the FATF's and FSF's lists of NCCTs and OFCs.

<sup>17</sup> See *First Annual Small States Forum: Background Information Document*, September 25, 2000, accessible at [www.worldbank.org/smallstates](http://www.worldbank.org/smallstates).

some small states have become successful at providing both onshore and offshore financial services, and the Bank supports their efforts to ensure that their regulatory and supervision frameworks are in line with international standards. Through the CAS, the Bank identifies financial sector issues and outlines the role it will play to address them, working in close collaboration with the IMF and other partners.

### **Fiduciary and safeguard rules**

19. The Bank has also tightened its fiduciary safeguards to ensure that its own lending is used for the purposes intended and not be subject to financial abuse. For project lending, the Bank asks borrowers to comply with well-specified requirements to ensure financial accountability and abuse prevention of funds made available by the Bank. For adjustment lending, in addition to safeguards for its own funds, the Bank works with countries to strengthen their overall public financial management. The number of country financial accountability and procurement assessments is growing quickly, and the procurement and financial management capacity of all implementing agencies is assessed before investment projects are presented to the Board for approval. Similarly, when extending loans or guarantees, or investing in equity instruments, IFC and MIGA follow international best practice based on their extensive experience, and apply rigorous scrutiny to projects in countries unfavorably rated by the FATF or the FSF.

20. The Bank Group is particularly attentive to structure its own financial operations, be they Bank's, IFC's or MIGA's funding, investment or derivative transactions, in a way that does not inadvertently undermine international efforts to curb money laundering. Although Bank practices are not jurisdiction-specific, they reflect the high standards of care and due diligence with which the Bank Group operates to mitigate risks, including reputational risk. Internal risk management guidelines limit Bank's financial transactions to counterparties with credit ratings of "A" or better. In addition, the Bank has a specific prohibition on the maintenance of deposits in OFCs, primarily out of concern with reputational risks, and investment activities are limited to instruments with ratings of "A" or better. In borrowing activities, the Bank deals only with reputable and well-established underwriters. Similarly, IFC's Treasury activities are subject to stringent guidelines approved by its Finance Committee and, in the case of liquid assets investments, investment authority approved by the Board. Currently, about 80 percent of securities held in the IBRD/IDA/MIGA portfolios are issued by governmental entities, with the remainder in Asset Backed Securities.

### **C. Fund/Bank Joint Work**

21. The Fund and the Bank have been contributing jointly to the countering of financial system abuse in the context of FSAP and ROSC program.

22. **The Financial Sector Assessment Program**, introduced in 1999, aims to identify both financial vulnerabilities and development needs. At the most general level, joint Fund/Bank FSAP work reduces the opportunities for financial crime through improving financial supervision and the preconditions (legal, governance, administrative, etc.) for

effective regulation and supervision. More specifically, FSAPs assess, by examining supervisory core principles, the susceptibility of the financial system to financial crime and money laundering, for example, because of excessive bank secrecy laws. All FSAPs include an assessment of BCPs (in particular CP15, which relates directly to money laundering); most contain assessments of the equivalent IOSCO and IAIS principles. The principle findings from the FSAPs are communicated to the Fund's and Bank's Executive Boards in the form of a Financial Sector Stability Assessment report (FSSA) and a Financial Sector Assessment report. As of end-March 2001, 14 FSSAs and nine FSAs have been issued to Executive Directors.

23. In the area of anti-money laundering, advice and recommendations arising from FSAPs include (i) introduction of legislation to do away with anonymous banking accounts; (ii) improvements to "know-your-customer" procedures in the context of the assessment of BCP 15; (iii) modifications to secrecy legislation to verify implementation of know your customer requirements; and (iv) implementation of new anti-money laundering laws.

24. The IMF and the Bank have also been collaborating closely in assessing progress in implementing selected international standards through the program on Reports on Observance of Standards and Codes. The international community has emphasized the development and implementation of standards as one of the key elements in strengthening the architecture of the international financial system by promoting the sound functioning of members' economic and financial systems. The assessment and disclosure of observance of standards can highlight potential vulnerabilities, help national authorities in their efforts to strengthen domestic economic and financial sector policy frameworks, and promote transparency and market discipline. Largely in the context of the FSAP, the Bank and the Fund conduct assessments of relevant financial sector standards (the Basel Core Principles, the IOSCO Principles and the IAIS Principles) that lead to the preparation of ROSCs. As of end-March, 2001, 38 ROSC modules in these three areas have been completed for 23 countries, of which 21 have been published.

### **III. INTERNATIONAL EFFORTS TO COUNTER MONEY LAUNDERING**

25. Several international organizations and task forces are involved in efforts to counter money laundering. They can be divided into (i) those that are concerned primarily with financial/supervisory matters, including (in addition to the Fund and the Bank) the Basle Committee, the IOSCO, and the IAIS; (ii) those that are concerned with both financial/supervisory and legal/criminal enforcement matters, including the FATF, the various regional anti-money laundering task forces, the United Nations, the Council of Europe, the European Union, the Organization of American States, and the Commonwealth Secretariat; and (iii) those that are primarily concerned with legal/criminal enforcement matters, including the Egmont Group of Financial Intelligence Units and Interpol. This

section briefly discusses those groups whose purview includes legal/criminal enforcement matters.<sup>18</sup> A summary of the nature and activities of these groups is found in Table 1.

Table 1. International Organizations Engaged in Anti-Money Laundering Activities

Organization	Operational Standard	Legally Binding	Membership	Focus	Implementation
FATF	FATF 40 Recommendations	no	mostly industrialized countries	prevention and enforcement	mutual evaluation
	25 Criteria	no			one way evaluation
Regional anti-money laundering task forces	FATF 40	no	open to jurisdictions in the region	prevention and enforcement	mutual evaluation
UN Global Program	Treaties	yes	most countries	enforcement	UN General Assembly
	Model laws, other sources	no		prevention and enforcement	surveillance and technical assistance
Council of Europe C.E. Committee	Treaty	yes	largely council membership	enforcement	Council of Europe
	Various sources	no		prevention and enforcement	technical assistance
EU	Directive	yes	EU	mostly prevention	EU Commission
O.A.S. C.I.C.A.D.	Model regulations	no	O.A.S. members	prevention and enforcement	technical assistance
Commonwealth	Model law	no	commonwealth members	prevention and enforcement	technical assistance
Egmont Group	Model agreement	no	diverse membership	enforcement	technical assistance and mutual assistance in investigations
INTERPOL FOPAC	Various sources	No	most countries	enforcement	mutual assistance in investigations

26. **The Financial Action Task Force's** 40 Recommendations are widely recognized as the key set of standards to deter the crime of money laundering. These recommendations involve both financial/supervisory and legal/criminal enforcement matters. FATF members evaluate their compliance with these crime-fighting standards through self-assessment and mutual evaluation exercises. These latter exercises involve standardized questionnaires, checklists, and on-site evaluations, and result in reports identifying weaknesses and areas for improvement. In addition, the FATF has produced a set of 25 Criteria Defining Non-Cooperative Countries or Territories (NCCTs), based on, but not identical to the FATF 40,

<sup>18</sup>These groups are described in greater detail in Annex I.

which it has used to evaluate 29 non-FATF members. The evaluations identified weaknesses and grouped countries based on their degree of compliance, and a list of NCCTs has been published. Various **regional anti-money laundering groups** (including the Caribbean FATF, Asia Pacific Group, the Latin American group GAFISUD, and the Eastern and Southern Africa Anti-Money Laundering Group) have endorsed the FATF 40 Recommendations, and also carry out mutual evaluations similar in nature to those of FATF members.

27. The two **United Nations**-sponsored treaties concerning money laundering focuses primarily on legal/criminal enforcement matters, addressing the matter of international cooperation in particular.<sup>19</sup> While generally consistent with the FATF 40, they often are more detailed. As part of a program in technical assistance, the **UN Global Program Against Money Laundering** has promulgated model laws that, while consistent with the FATF 40, address both financial/supervision and legal/criminal enforcement matters in greater detail; The Global Programme closely follows developments in UN Member States with a view to identifying areas of need for anti-money laundering technical assistance. In addition, both the **Organization of American States Inter-American Drug Abuse Control Commission** (CICAD) and the **Commonwealth Secretariat** have prepared model laws that address both financial/prevention and legal/criminal matters. At their meeting in September 2000, the **APEC Finance Ministers** called for the creation of an APEC working group to conduct a survey of the domestic legal and regulatory frameworks for fighting financial crimes, and to report to the Ministers' meeting in September 2001.

28. The **Council of Europe**-sponsored anti-money laundering treaty also focuses primarily on legal/criminal enforcement matters and, like the UN models, is both consistent with, though more detailed than, the FATF 40. The Council's **Select Committee of Experts on the Evaluation of Anti-Money Laundering Measures** (PC-R-EV Committee) undertakes voluntary evaluation of compliance with the Treaty (as well as with the FATF 40) and provides technical assistance in improving anti-money laundering policies. The current **European Union** anti-money laundering Directive is primarily concerned with financial/supervision matters, and is consistent with the original, but not the current, FATF 40; a draft proposed amendment would bring the standards in line with the current FATF 40. The EU Commission is charged with ensuring compliance with EU Directives.

29. The **Egmont Group of Financial Intelligence Units** model agreement on information sharing among jurisdictions is the most important standard on this topic. It is both consistent with the FATF 40 and more detailed. The Egmont Group also provides technical assistance on the design and implementation of financial intelligence units. The **Interpol Bureau des Fonds Provenant d'Activités Criminelles** (FOPAC) is the main

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<sup>19</sup> The two treaties are the UN Conventions (i) Against Illicit Traffic in Narcotics Drugs and Psychotropic Substances (the Vienna Convention), and (ii) Against Transnational Organized Crime (the Palermo Convention).

institution coordinating international anti-money laundering investigations, and has considerable expertise in the legal/criminal enforcement areas. It provides technical assistance in drafting and implementing laws relating to criminal enforcement.

30. The efforts of these groups have resulted in widespread recognition of the seriousness of the problem of money laundering, and in the adoption, by over 100 countries, of various types of anti-money laundering laws. Each of these groups accepts the primary importance of the FATF 40 as a key standard for anti-money laundering policies. However, mandates, memberships, and focuses of these groups vary. As a result, the details with respect to standards used by them vary also, as do their methods of assessment or assistance to improve compliance. There is scope for more effective coordination of international activities against money laundering. Such coordination could focus on the recognition of modalities for assessing anti-money laundering principles and on the identification and delivery of technical assistance. The Fund and the Bank, within their fields of competence, could play a useful role in such coordination efforts.

#### **IV. ENHANCING CONTRIBUTIONS TO COMBATING MONEY LAUNDERING: ISSUES FOR THE FUND AND THE BANK**

31. The breadth and cross-cutting nature of the global agenda to curb money laundering calls for a cooperative approach among many different international institutions. International efforts against money laundering are led by the relevant specialized institutions, notably the FATF, the regional anti-money laundering groups and the UNDCP. The Bank and Fund's work in financial sector areas has complemented anti-money laundering efforts, while remaining within their respective mandates and areas of expertise.

32. The Fund and the Bank can increase their participation in the global fight against financial abuse and money laundering by (i) publicizing both the need to put in place the necessary economic, financial, and legal systems designed to protect against money laundering and the role that the Bank and the Fund are playing in helping meet this need; (ii) recognizing the FATF 40 as a standard for anti-money laundering useful for Fund/Bank operational work, (iii) intensifying the focus on anti-money laundering elements in relevant supervisory principles, (iv) working more closely with the major international anti-money laundering groups, and (v) increasing the provision of technical assistance in this area. These proposals are discussed below and summarized in Box 1.

#### **Publicize the importance of countries acting to protect against financial abuse and money laundering**

33. The Fund and the Bank can publicize in general terms both the need to put in place the necessary economic, financial, and legal systems designed to protect against financial abuse and money laundering and the role that the Fund and the Bank are playing in helping meet this need. The IMFC and DC, as well as the Boards of the Fund and the Bank could

make appropriate public statements; the Fund and the Bank could better publicize their respective activities; and both institutions could undertake additional studies, engaging in workshops, focusing on the macroeconomic and development affects of money laundering.

**Box 1. Steps to Enhance the Fund's and Bank's Contribution to International Efforts Countering Money Laundering**

- ***Publicize importance of countries acting to protect against financial abuse and money laundering.*** The IMFC and DC, as well as the Boards of the Fund and the Bank, to make appropriate public statements; the Fund and the Bank to publicize relevant information on their activities; and both to undertake additional studies, engage in workshops etc. with respect to the macroeconomic and development affects of money laundering.
- ***Recognize the FATF 40 as a standard for anti-money laundering useful for Fund/Bank operational work.*** The FATF (and possibly regional groups) could be invited to prepare a ROSC module provided that the underlying ROSC process is observed, i.e., that there is uniformity of treatment, the FATF 40 is used for all assessments (including FATF non-members) and the approach to assessments is cooperative and voluntary. At this time the conditions for the ROSC process are not met and therefore the staffs do not recommend that FATF (or other groups) be invited to prepare ROSC modules.
- ***Intensify focus on anti-money laundering elements in relevant supervisory principles.*** The Fund and the Bank to develop a methodology document for determining compliance with key anti-money laundering elements in the relevant BCP, IOSCO and IAIS principles (see Annex II). The methodology document would draw from guidance material available from relevant organizations/entities, including Basel Committee, IOSCO, IAIS and the FATF. (About half of the FATF 40, which pertain to financial/supervisory matters, would be relevant in crafting the methodology document.) Detailed assessments could be published or shared with the FATF and other regional anti-money laundering task forces.
- ***Work more closely with major international anti-money laundering groups.*** The Fund and the Bank would work more closely with other international anti-money laundering groups, including participating in more meetings and joint workshops, and exchanging information, particularly on compliance with financial standards. To avoid confusing different purposes and methods, the Fund and the Bank would not undertake joint missions with the FATF or regional task forces.
- ***Increase the provision of technical assistance.*** The delivery of TA by the Bank and the Fund when combined with other bilateral and multilateral TA providers would achieve greater efficiency and effectiveness.

34. The Boards of the Fund and the Bank could seek a statement by IMFC and the DC that would (i) recognize that money laundering is a global concern requiring concerted and cooperative action on the part of a range of institutions, with the lead taken by the FATF and the UNDCP,<sup>20</sup> that effective anti-money laundering measures are important to all Fund and Bank members (though especially to those with large financial markets) and that implementing such measures is a primary responsibility of national authorities; and (ii) encourage the Fund and the Bank to enhance their current contributions to counter money laundering by helping countries strengthen their economic, financial and legal systems broadly.

35. Next, the Fund and the Bank could communicate to the public more effectively their various contributions to preventing financial abuse and money laundering. They could do this by emphasizing in their public outreach activities the role that the institutions play, through support of economic programs and technical assistance in helping countries to develop and reform their financial systems and assisting them towards putting in place a proper regulatory and supervisory environment. In particular, the activities with respect to financial sector standards and codes assessed by the Fund and the Bank could be stressed. Methods for improving outreach could include speeches, articles, and seminars.

36. The Fund and the Bank could undertake additional research into the macroeconomic and development effects of financial crime and money laundering. Because the scale and consequence of financial sector abuse in general, and of money laundering in particular, are not well understood (for the obvious reason that illegal activities are difficult to measure) such additional research would be difficult. At a minimum, however, the research would review effects of financial crime on the macro economy and would aim at providing an indication of the significance with which crime impacts industrial and developing country markets. The output of such research could be brought together in 2002 in a paper for both the Fund and Bank Boards.

### **Recognize the FATF 40 as an international anti-money laundering standard**

37. The Fund and the Bank could recognize the FATF 40 as the internationally accepted standard for anti-money laundering policies useful for Bank and Fund operational work, which would increase the number of recognized standards to 12. The FSF already includes the FATF 40 among its 12 key standards for sound financial systems. In deciding to recognize the FATF 40, Directors could consider the relevance of the FATF 40 to macroeconomic stability and financial soundness. Directors may also wish to consider whether the FATF 40 are broadly recognized as an international standard,<sup>21</sup> and if they are

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<sup>20</sup> Recognizes the key anti-money laundering statements, including the FATF 40, the UN Conventions Against Illicit Traffic in Narcotics Drugs and Psychotropic Substances (the Vienna Convention) and Against Transnational Organized Crime (the Palermo Convention) and the relevant UNDCP model laws; and invitations to members to abide by these principles.

<sup>21</sup> Other internationally recognized money laundering standards are discussed in Section II.

appropriate for developing as well as developed countries.<sup>22</sup> In this context it should be noted that the FATF recommendations have become dated and that, as a result, the FATF is revising its existing 40 recommendations to reflect the evolution of money-laundering activities and to address inconsistencies in the treatment within the FATF membership and vis-à-vis non-members. The process of revising the FATF 40 Recommendations is likely to extend beyond 2001. The FATF 40 is not, however, the only standard undergoing revision.

38. With respect to assessment, neither the Fund nor the Bank could be expected to assess compliance with those aspects of the FATF 40 that relate to legal/criminal enforcement matters.<sup>23</sup> One possibility would be for the Fund and the Bank to assess only those aspects of the FATF 40 relating to financial/supervisory matters. However, an expert from the UNDCP stated—most recently at the February workshop—that the FATF 40, while covering many areas that are primarily financial/supervisory in nature, were designed to be assessed as a unified whole. Separating out those principles that concerned legal/criminal enforcement matters from financial regulation and supervision would be problematic in his view.

39. One possibility would be to invite the FATF (perhaps in cooperation with regional task forces and other anti-money laundering organizations) to assess compliance with the FATF 40. FATF would prepare a ROSC module on anti-money laundering provided that established Bank-Fund guidance for incorporating standards as ROSCs were observed. The FATF and the regional groups are already carrying out assessments of compliance with the FATF 40 Recommendations.<sup>24</sup> However, the FATF has applied the FATF 40 when conducting mutual evaluations of its members, but the FATF has used the FATF 25 Criteria, to assess jurisdictions that are not FATF members<sup>25</sup>. Evaluations by the FATF of non-members are involuntary and involve a “name and shame” approach to induce compliance. The FATF is also considering the possibility of recommending that sanctions be imposed on non-complying jurisdictions in some circumstances.<sup>26</sup> For ROSCs, a single international

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<sup>22</sup> In the *Summing Up by the Acting Chairman Assessing Implementation of Standards—A Review of Experience and Next Steps* (SUR/01/13)(29/1/01), a number of Directors expressed concerns of ownership and of ensuring that all members had a role in shaping and guiding work on standards. In this context, Directors may wish to note that the FATF 40 were drafted primarily by the industrialized countries.

<sup>23</sup> At the July 2000 discussion of OFC assessments (*Concluding Remarks on Offshore Financial Centers and the Role of the Fund*), Directors noted that law enforcement measures were not appropriate for the Fund to assess.

<sup>24</sup> It should be noted that these task forces have very small secretariats, and that evaluations are conducted by national experts from FATF and regional group members, including law enforcement personnel.

<sup>25</sup> See Annex 1 for a description of the differences between the FATF 25 Criteria and the FATF 40 Recommendations

<sup>26</sup> Among the sanctions envisaged by FATF are financial restrictions by members of FATF that could be in violation of Article VIII 2(a) of the Fund’s Articles. Staff have spoken to FATF Secretariat to make this point, in the expectation that FATF will find alternative approaches.

standard□such as the FATF 40□should be applied in a uniform fashion and on a voluntary basis.<sup>27</sup>

40. Because the FATF process lacks conformity with the principles of the Bank-Fund ROSC initiative, the two staffs recommend that FATF would not be invited at this time to prepare a ROSC module on the FATF 40. Instead, the two staffs could contribute to the ongoing revision of the FATF 40 and discuss with the FATF the principles behind the ROSC procedures, and come back to the Board with a report and recommendations.

### **Intensify focus by the Fund and the Bank on relevant anti-money laundering principles**

41. Independent of a decision to recognize the FATF 40 as a standard for operational work, the Fund and the Bank could deepen the emphasis on anti-money laundering elements of the BCP, IOSCO and IAIS Principles, which are already assessed under the FSAP. Observance of these and other principles helps ensure that financial institutions have in place needed management and risk control systems, which are crucial in helping to prevent financial crimes, including money laundering. The Fund and the Bank could deepen their assessment of compliance with the anti-money laundering elements of BCPs and the IOSCO and IAIS principles drawing on a new methodology document (to be developed) that sets out criteria for assessment and procedures for preparation of the report. Such a methodology document, while not directly using the FATF 40 as a standard, would cover the essence of the FATF 40 relating to financial/supervision matters (about half of the FATF 40).<sup>28</sup> Using the methodology document, a focused assessment of relevant anti-money laundering elements will be included as part of the detailed assessments of compliance with BCPs, IOSCO and IAIS Principles.

42. The release of detailed assessments, including the focused assessment of relevant anti-money laundering elements, would follow the policy established for technical assistance reports. In addition, the country concerned could share the reports with the FATF and other regional anti-money laundering task forces. Because of the Fund and Bank’s comparative advantage in the financial sector, the detailed assessments could reduce the burden on the FATF and other anti-money laundering groups by limiting duplication of efforts.

43. As more FSAPs are undertaken, the coverage of anti-money laundering issues in financial sector work will deepen. In line with the Fund and Bank Executive Boards’ guidance, the schedule for FSAPs should give the highest priority to systemically important

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<sup>27</sup> “[A]ssessments must be independently conducted and consistently applied across all countries” *Summing Up by the Acting Chairman Assessing Implementation of Standards□A Review of Experience and Next Steps* (SUR/01/13)(29/1/01).

<sup>28</sup> See Annex II: FATF 40 Recommendations on the Principles of Supervision. That document could draw on those standards and principles currently used by other international task forces and groups that deal primarily with financial/supervisory matters.

countries. The Fund and the Bank would send a clear signal of the importance of effective anti-money laundering measures for national financial systems and the international financial system. It would also emphasize that both the Fund and the Bank are giving heightened attention to governance as an important factor influencing economic performance.

### **Work more closely with major international anti-money laundering groups**

44. The Fund and the Bank could work more closely with other international anti-money laundering groups and task forces. The most important of these are the FATF and the regional anti-money laundering task forces. Fund and Bank staff attend the main FATF meetings and now also some of the regional groupings.<sup>29</sup> Staff could work more closely with FATF by playing a role in the current substantial revisions to the FATF 40 and exchanging information, particularly on compliance with financial standards. On the sharing of information, FATF has already agreed to share results from their exercises with Fund and Bank staff conducting financial assessments, for example in the context of FSAPs.<sup>30</sup> In addition, Bank and Fund members that have undergone assessments could voluntarily share information on the observance of relevant principles with FATF. Such exchanges would eliminate some duplication between FATF and Bank and Fund assessments, and improve the quality and timeliness of assessments by both institutions. The staffs do not propose to undertake joint missions with the FATF or regional task forces.

### **Increase the provision of technical assistance**

45. The Bank and the Fund could help countries improve their anti-money laundering laws and practices through the provision of technical assistance. At present, TA for anti-money laundering is provided bilaterally (especially from FATF members), by the UNDCP, Egmont Group, INTERPOL, and to a more limited extent through the capacity building of the Bank, the Fund and other multilateral agencies. Bank and Fund staff should coordinate more closely with these other TA providers, sharing knowledge and experience (within the confines of confidentiality protocols) wherever possible.

46. In the context of their regular activities, the Fund and the Bank already solicit information on TA and training needs to enhance countries' capacity to strengthen adherence to international standards, including in some areas directly pertinent to countering financial sector abuse and specifically money laundering. To assess comprehensively the scale of needed resources (human and financial), however, would require an evaluation of

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<sup>29</sup> The Fund is also an observer at the Asia/Pacific Group on Money Laundering, at the African group (GIABA) and at the Council of Europe Select Committee of Experts; it is not an observer at any of the other three regional FATF-type meetings: Caribbean (CFATF), Eastern and Southern Africa Group (ESAAMLG), and South American (GAFISUD). The Bank is an observer at the Asia/Pacific Group on Money Laundering, the Council of Europe Select Committee of Experts, and the two African groups (GIABA, and ESAAMLG).

<sup>30</sup> All sharing of information from the FATF with the Fund or the Bank is on a case-by-case basis and only with the prior consent of the country concerned.

institutional and legal infrastructure. The G7 has offered to provide TA to jurisdictions that commit to make improvements in their regimes to counter money laundering.<sup>31</sup> The Fund and the Bank have been asked to play a role in coordinating this effort. Such an assessment of TA needs, coordination of TA delivery, and direct provision of TA would represent a significant resource commitment for the Fund and the Bank that would take both institutions into areas outside their expertise and mandates. The Boards need to consider whether they want the Fund and the Bank to (i) increase TA in relevant prevention areas; (ii) identify TA needs for addressing money laundering issues; or (iii) coordinate all TA on money laundering, i.e., also in law enforcement areas. A preferred option would be to increase TA in relevant prevention areas, with the extra work by the Fund and the Bank focusing on adherence to relevant standards (outside law enforcement). More general TA and coordination of all money laundering TA would probably be best left to the FATF, the UN and others.

47. **Priority for countries listed as NCCTs.** The FATF has proposed to give priority for TA to jurisdictions identified as NCCTs. Although the NCCT list is published, the NCCT process is not fully transparent and deliberations determining whether to list jurisdictions are held in closed sessions. Some of these jurisdictions are on the schedule of OFC assessments. In general, however, assessment of TA needs and of other support would be available to the entire membership (i.e., would not be targeted at specific groups, e.g., OFCs, listed NCCTs) and could, within the context of the Fund's and Bank's priorities for TA and resource availability, respond to those where financial abuse and money laundering are a significant policy issue.

## V. RESOURCE IMPLICATIONS

48. The resource implications of the Bank and Fund contributions to the international efforts against money laundering cover four broad areas: (i) extra diagnostic work including through FSAP, ROSCs and OFC assessments; (ii) extra work on surveillance and program countries; (iii) closer collaboration with FATF and the regional task forces; and (iv) the delivery of technical assistance. Table 2 breaks out the staffs' resource estimate by area, which for the Fund equates to roughly five extra staff years and for the Bank an extra annual cost of US\$600,000. Staff notes that resource estimates are tentative, particularly with regard to distribution among the four broad areas. Firmer estimates would be possible as experience is gained.

49. For the Fund and Bank, the decision on how to rank this work within overall priorities and whether and how to ensure appropriate staffing and funding for this work would need to be considered as part of their respective budget reviews and discussions, which could entail requests for supplemental budget resources and for the mobilization of appropriate external

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<sup>31</sup> See Statement of the Group of Seven Finance Ministers and Central Bank Governors, Palermo, Italy (February 17, 2001), EBD/01/20 (February 20, 2001).

resources. The Fund and the Bank would continue to use experts from cooperating institutions (with a dollar cost to the Fund and the Bank, as well as an opportunity cost to the institutions concerned), but would also need to provide the infrastructure to support this TA program.

50. Not included in the estimate is the anticipated work involved in incorporating the anti-money laundering standards into the Bank and Fund diagnostic work, in particular, the development of appropriate templates and methodology. This would entail perhaps one an additional one staff year in the first year.

Table 2. Additional Staff Resources for Anti-Money Laundering Work

	IMF Number of staff weeks	Bank Budget thousand dollars 1/
FSAP and OFC assessments	60	150
Technical assistance, capacity building, and additional diagnostic work	60	300
Collaboration with FATF, the regional task forces and other related organizations, as well as research	40	150
Surveillance and program countries	40	Not applicable
Total	200	600

<sup>1</sup> Bank staff are examining the possibility for redeployment to cover this cost.

51. FSAP and OFC assessments would include additional diagnostic work analyzing the relevance of money laundering to the macro-economy, reviewing related legislation, meeting with officials in charge, assessing implementation of the corresponding Basel, IAIS, and IOSCO principles, and summarizing the findings of these assessments. In fiscal year 2002, 24 FSAPs and 7 OFC (Module 2 and 3) assessment missions are planned, which would require about ten additional staff days each, including for the preparation of the report.

52. An important incremental cost would include the delivery of technical assistance and support for capacity building that results from the FSAP and OFC missions. Technical assistance missions and capacity building support would be also provided to countries and jurisdictions where money laundering is an identified concern, but for which a mission would not have been anticipated under the FSAP or OFC initiative. Fund staff would anticipate an extra 15 missions a year, each lasting two weeks in the field and two further weeks at headquarters. (TA would continue to be available from other providers.) In the case of the Bank, a significant proportion of this cost would be included in and covered by redeployment within regular country programs.

53. Closer collaboration with FATF, FATF-style bodies and other related organizations means staff attendance at more meetings. The Fund and the Bank would mainly increase their participation in appropriate FATF proceedings, notably in the review process of the

FATF 40 recommendations and in the definition of assessment methodology and procedures for FATF assessments. The Bank and Fund would need to develop a closer cooperation with international and regional anti-money laundering bodies, in which they already have observer status. Also captured in this resource category are additional costs associated with research of financial abuse and money laundering.

54. The extra amount of time required on surveillance and program missions and subsequent follow-up, which would only apply to the Fund, is difficult to estimate, since it is likely to vary greatly between countries. This work might require an additional staff year.

## **VI. ISSUES FOR DISCUSSION**

### **For Fund and Bank Directors**

55. Do Directors consider that financial abuse (including money laundering in particular) is a major threat to the development and stability of financial systems and institutions of members?

56. Do Directors agree that the Fund and the Bank are already making significant contributions to members' efforts to prevent financial abuse, including money laundering, through their enhanced efforts to help members strengthen their economic, financial and legal systems, as set out in Section II of the paper? Do Directors agree that international anti-money laundering efforts should be reinforced by more intensive efforts by the Fund and Bank?

57. Do Directors agree that the Fund and the Bank can play a complementary role in global anti-money laundering efforts by intensifying their work, as set out in Box 1? In particular, do Directors agree that ongoing financial sector work, including FSAP, should be used as a vehicle for assessing more closely compliance with the supervisory principles relevant to anti-money laundering? If so, do Directors agree that the staffs' recommendation provides a suitable way to accomplish this goal?

58. Do Directors consider that the existing FATF 40 Recommendations should be recognized by the Fund and Bank as an anti-money laundering standard useful for their operational work?

59. Do Directors agree that at this time the FATF (as well as other bodies engaged in anti-money laundering efforts) should not be invited at some point to prepare a ROSC module?

60. How do Directors view the proposals for closer cooperation with FATF and other bodies engaged in anti-money laundering efforts, for example, through participation in the review of the FATF 40, and in FATF-style regional groups?

61. Do Directors agree that the Fund and the Bank should strengthen their policy dialogue with members on relevant money laundering concerns and provide extra technical assistance and support for capacity building (in areas of their mandate and in line with Fund and Bank priorities for TA), as a complement to other international institutions' efforts?

62. Should the Fund and the Bank develop and publish more analytical work on financial abuse, notably money laundering?

**For Fund Directors**

63. Do Directors agree that the Fund should allocate additional resources to support the proposed increased participation by the Fund in international anti-money laundering efforts? How should the Fund mobilize these extra resources, from external sources?

64. Do Directors consider that cross border implications of money laundering should be raised by staff during the Article IV consultation for a given member even if it is not macro-relevant for that member?

**For Bank Directors**

65. Do Directors agree that the most important contribution that the Bank can make to global efforts to combat financial abuse is to help countries strengthen their structural and institutional underpinnings?

66. Do Directors agree that the joint Bank-Fund program to support anti-money laundering efforts outlined above is consistent with the Bank's development mandate and comparative strengths?