

## GOVERNANCE AND ILLICIT FINANCIAL FLOWS\*

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### Abstract

Insofar that it corrodes governance, engendering opportunistic crimes, grand corruption lies at the core of the problem of illicit financial flows. We identify at least two likely antagonistic circles in the illicit flow process—a virtuous circle and a vicious circle—both rooted in one common factor, namely, the strategic complementarity between corruption and governance. Also, we consider the scope of global governance architecture in encouraging banks to “do the crime, pay the fine, and do no time.” Given this structure, the observed, rampant impudence of banks’ participation in illicit financial flows is understandable and society would not be shocked should global mega-banks increasingly resemble a police establishment run by ex-convicts. Curbing illicit flows in such a circumstance would be daunting. Therefore, civil society must live up to its civic responsibilities by displacing the vicious cycle first through creating the right incentives for politicians to identify negatively with illicit financial flows.

**Key Words:** Capital flight; illicit financial flows; Africa; sub-Saharan Africa; governance; corruption

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## 1. Introduction

What does \$1,000 million or one billion dollars of stolen public money mean to the village blacksmith who molds farm hoes or sears cutlasses in a village in a poor developing country? Not much. Presumably, he is not able to get his head around such colossal amount of money, which in all likelihood does not exist in the numerology of his vernacular. By contrast, the following cost and benefit calculus is sure to capture the blacksmith's attention:

The amount of money an emir expends on a single trip to Europe for medical check-up would build a clinic big enough to serve a community of 5000 people; the amount of foreign exchange a top civil servant pays yearly to educate a single child abroad would build a primary school capable of providing basic education to hundreds of pupils; the amount of money a politician spends to sponsor his wives and children's trips to Saudi Arabia for lesser pilgrimage, to Dubai for shopping, and Europe for holidays annually is enough to establish community banks and provide access to capital for thousands of small businesses or fund poverty alleviation projects in several communities (Suleiman, 2012, p. 1).

In 2010, shortly before Suleiman (2012) expressed these views, the adverse consequences of illicit financial flows on economic transformation and human development in Africa were brought to the attention of regional policymakers by three economists, namely, Melvin Ayogu, Raymond Baker, and Léonce Ndikumana during a side event. More specifically, a panel discussion to alert policymakers to the problem was organized at the 43rd Session of the Commission/3<sup>rd</sup> Joint Annual Meetings of the Africa Union (AU) Conference of Ministers of the Economy and Finance and the United Nations Economic Commission for Africa (ECA) Conference of African Ministers of Finance, Planning, and Economic Development held in Lilongwe, Malawi, March 29–30, 2010. After examining the issues at

stake, conference participants called upon the ECA and the AU to lead the effort to combat illicit financial flows from Africa. Following a resolution passed by these ministers, a “High Level Panel on Illicit Financial Flows from Africa” (hereafter “High Level Panel”) was established by the ECA and inaugurated on February 18, 2012 in Johannesburg, South Africa<sup>2</sup> It is envisaged that the High Level Panel would work to increase collaboration and cooperation amongst African countries, their regional economic communities, and external partners to promote better global understanding of the scale of the problem for African economies as well as encourage the adoption of relevant national, regional, and global policies, including safeguards and agreements to redress the situation.

One should emphasize that although illicit financial flows create serious problems for the financing of development in many poor countries, including those in Africa, that fact alone does not guarantee that policymakers will take steps to curb the problem. Whether or not the problems of illicit financial flows attract the attention of governments depends crucially on the linkage(s) between the consequences of illicit financial flows and the political fortunes of policymakers (domestically and globally), including the interests of global actors.<sup>3</sup> Nowadays, global actors comprise individuals whose domicile is external to nation-states as well as those domiciled within nation-states who, in catering to global constituencies, necessarily play on the global platform.

In this connection, it is pertinent to note that some of the studies Ajayi and Ndikumana (2014), as well as others in the literature (Stephenson et al., 2011), suggest that the roots of illicit financial flows appear to lie in the structure of governance. We extend this idea by postulating that, although rooted in governance, the persistence of illicit financial flows depends on both domestic and international actors, and therefore on international political

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<sup>2</sup> Economic Commission for Africa (2012), p.1.

<sup>3</sup> For an elaboration, see for instance Ayogu and Gwatidzo (2011) and references therein.

economy, in addition to the structure and functioning of global (financial, legal, and political) organizations. Many argue that the drivers of illicit financial flows are rooted either in micro-foundational issues, such as the outcome of individual portfolio choices, or in macro-foundational issues, such as macroeconomic instability or low economic growth. On the contrary, some African countries have had more financial hemorrhage during periods of economic growth. For example, estimates of the size of illicit financial flows from Africa during the period 1970–2010 (Ndikumana and Boyce, 2012, pp. 19-22) show that primary commodity booms have been associated with higher illicit financial flows.

In line with our postulate that governance—global and local—is an essential element in curbing illicit financial flows, this paper explores the nexus between governance and illicit financial flows. It especially emphasizes that grand corruption is at the core of the nexus of governance and illicit financial flows, as it corrodes governance, which in turn engenders opportunistic crimes. Grand corruption is both a profitable predicate crime and a constraint to enforcement of rules. The analysis in this paper uncovers two antagonistic circles in the illicit flow process—a virtuous circle and a vicious circle, which are both rooted the strategic complementarity between corruption and governance: While good governance curbs corruption (the virtuous cycle), corruption corrodes governance because poor governance enables corruption (the vicious cycle). The analysis is supported by empirical evidence from the literature as well as illustrations from country case studies.

The rest of the paper is organized as follows. Section 2 discusses illicit financial flows in greater detail to strengthen our appreciation of the phenomenon and clarify some key concepts associated with it. Section 3 defines governance as used in this study and develops an understanding of the linkages between governance and illicit financial flows. Section 4 concludes and suggests crucial next steps in the fight against illicit financial flows.

## 2. Definition, typology and scale of illicit financial flows

As the review in Ajayi and Ndikumana (2014) makes clear, the depth and scope of the literature on illicit financial flows in developing countries, including those focusing on Africa, is thin. However, the Afrocentric strand— Kar and Cartwright-Smith (2009), Ndikumana and Boyce (2003, 2011), and Boyce and Ndikumana (2001)—has made significant progress in measuring the scale of the problem. Without serious scholarship on measurement, creating awareness of the problem would have been more difficult due to its clandestine nature, which lends itself conveniently to the denial of its existence. Therefore, the contributions of previous studies that have sought to quantify the scale of illicit financial flows cannot be understated.

Besides the literature on illicit financial transfers from African economies, several studies examine the phenomenon from a global perspective (Reuter and Truman, 2004; Baker, 2005). Within this genre, there are more specialized studies, such as those that pursue tax justice and target tax dodgers.<sup>4</sup> Others, such as those undertaken by the United Nations Office on Drugs and Crime (UNODC) and the World Bank (2007, 2009), World Bank and UNODC (2011), UNODC (1998) as well as Basel Institute on Governance (2009) pursue initiatives to assist countries and communities, particularly developing countries, recover monies illegally transferred from national treasuries by public officials and their co-conspirators.

Baker (2005, p. 23) defines illicit financial flows as “dirty money,” and dirty money as “money that is illegally earned, illegally transferred, or illegally utilized.” He argues that “[i]f it breaks laws in its origin, movement, or use, then it properly merits the label.” Some readers may not agree with this definition, noting that some “dirty money” may not cross national boundaries and therefore may not actually leave the economy or jurisdiction where the

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<sup>4</sup> For a description, see Shaxson (2011).

illegality occurred. If the money changes ownership (e.g., it is stolen from the national treasury) but remains in the country, it is likely that the affected economy will not be deprived of development capital. Thus, they argue that unless the money is transferred outside the country (e.g., into an offshore account or invested in assets abroad), the criminalized economy may not be subjected to the developmental consequences of illicit financial flows. We need to be careful here. Money that changes hands from a legitimate owner to one who illegally possesses it may still have negative consequences for the economy even if the money is not taken out of the country. Individuals who steal money from the government treasury (i.e., grand corruption) may be afraid to invest it openly and hence, may not be able to undertake the types of investment projects that contribute to job creation and economic growth.<sup>5</sup>

It is useful to make a careful distinction between dirty money and illicit financial flows for the purpose of policy prioritization and the selection of appropriate intervention strategies. Having appropriate conceptual understanding of the typologies of illicit financial flows and their characteristics is also important in gauging the accuracy of estimates of the magnitude of the flow, particularly as there are very limited means of judging the robustness of the estimates. Consider, then, the example of a citizen who earns a salary legitimately, purchases a gun, and commits a crime. Does this make his salary or payment to a licensed firearm retail outlet dirty money or an illicit financial flow? Our point is that dirty money of the illicit financial flow genre is a subset of all dirty money.

In their seminal contribution to the dirty money literature, Reuter and Truman (2004, p. 1) do not define dirty money explicitly. Instead, they refer to its obverse, money laundering, which they define as “the conversion of criminal incomes into assets that cannot be traced back to

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<sup>5</sup> We are indebted to John Mbaku for this insight.

the underlying crime.” Thus, illegality (why you move money) rather than flows (how you move money) is of essence in their characterization. In this framework, where the funds are located is not as crucial perhaps as the source of the monies.

Other important contributions to the literature on illicit financial flows have come from Global Financial Integrity (GFI), a Washington, D.C.-based organization that heads the Task Force on Financial Integrity and Economic Development, which was established in January 2009 by a global coalition of civil society organizations and several national governments “seek[ing] greatly improved financial transparency and accountability on an international level.” The Task Force has been renamed The Financial Transparency Coalition (2013).<sup>6</sup> GFI pursues this goal through original research and by advocating for greatly improved transparency and accountability in the global financial system. In their analysis, Kar and Cartwright-Smith (2009) of Global Financial Integrity use the definition in Baker (2005), but one of the authors of the report, Dev Kar, has elsewhere defined illicit financial flows as involving “the cross-border transfer of the proceeds of corruption, trade in contraband goods, criminal activities, and tax evasion” (Dev Kar, 2011, p. 3). His definition is useful because it is operational and circumscribed, captures the essence of the definition of dirty money in Reuter and Truman (2004), and can be applied for the purposes of policy intervention and legal remedies. Since it is both operational and circumscribed, it is also useful in understanding the scope of illicit financial flows.

In spite of the diversity of views on the nature of illicit financial flows, there is some agreement in the literature around the scope of illicit financial flows in Africa, emphasizing two critical parameters identified in Dev Kar (2011), namely, cross-border movements and the nature of the money. In other words, the provenance of the money and how it is moved

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<sup>6</sup><http://www.financialtransparency.org/about/overview/>

are important. To the extent that the origin of the money can be expected to influence the decision on how the money is moved, the pattern of behavior defined by the acquisition and the manner of transfer is informative in trying to establish the nature of a financial flow. Table 1 uses a 2x2 matrix of dimensionality to classify the nature of a financial flow.

**INSERT TABLE 1 HERE**

We would like to reinforce the discussion of the nature of financial flows by drawing lessons from an important legal precedent. In *Cuellar v. United States*, 553 U.S. 550 (2008), a case that was heard on appeal to the U.S. Supreme Court involving the provision of money laundering statute 18 U.S.C. §1956(a)(2)(B)(1) prohibiting international transport of the proceeds of unlawful activity. Regaldo Cuellar was arrested and charged with money laundering after police found nearly \$81,000 hidden in a secret compartment beneath the floorboard of a car that he was driving through Texas to Mexico. Cuellar was later convicted of money laundering but an appeals court overturned the conviction. The appeals court held that in order to secure a conviction under the federal money laundering statute, the government had to prove that the defendant was trying to depict the money as “legitimate wealth,” not merely show that the defendant tried to hide it. The government appealed to the U.S. Supreme Court. The unanimous opinion was written by Justice Clarence Thomas. The Court overturned Cuellar’s conviction and held that the money laundering statute does not contain a “legitimate wealth” requirement and that the mere proof that a defendant had attempted to conceal the money is not enough to uphold a conviction for money laundering. Referring to the language of the statute, the Court stated that the government needed to prove

that in transporting the money, the defendant intended to conceal, not just the money, but also the nature, location, source, ownership, or control of the money.<sup>7</sup>

But why are money laundering and the requirements for establishing the crime in the United States important for the fight against illicit financial flows from Africa? Specifically, why are legal precedents in the United States and other countries pertinent to the fight against illegal money transfers in Africa? Beginning with the latter question, foreign legal precedents matter because illicit financial flows of relevant in Africa are predominantly international phenomena. Since the transport of stolen monies or illegally-obtained assets across national borders involves multiple jurisdictions, the effective control of such activities cannot be undertaken without the consideration of the interdependencies inherent in the process. Effective and full prosecution of money laundering cases usually involves tracing and identification, a process that may require interface with multiple jurisdictions, which in turn requires an understanding of their protocols.

To the question of why money laundering is archetypical, it should be noted that it, as a business, stands at the epicenter of the entire criminal enterprise because a criminal's ultimate desire is to legitimize the payoff from crime; for that is when crime really pays. In other words, when a criminal can successfully distance the crime from the proceeds (dirty money), yet have unfettered access to the clean transform of the dirty money. Mindful of this aspiration, law enforcement authorities in the United States have made money-laundering charges a potent prosecutorial tool (Leibman, 2010). The charges "generally carry far more severe sentencing exposure" (Leibman, p. 1) than the underlying transgressions (predicate offenses) that generated the proceeds. Conviction for money laundering also allows prosecutors to threaten forfeiture of the stolen money or its transform, all of which happen to

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<sup>7</sup> We thank John Mbaku for elaborating the essence of the burden of proof as required by the law.

be important points to consider in stolen asset recovery initiatives in developing countries. Therefore, measures that diminish money laundering also lower the likelihood of illicit financial flows.

Baker (2005, pp. 49, 72) identifies three major types of illicit financial flows based on the perceived extent of potential criminality of the activities: (1) near-universally accepted criminal activities; (2) conditionally criminal activities; and (3) unlawful activities that are not universally criminal, but carry that potential depending on the jurisdiction. Predicate crimes, such as drug dealing, bank fraud, and terrorism, are elements of near-universally-accepted criminal activities. Bribery and corruption are elements of conditionally criminal activities simply because the type of behavior that qualifies as corruption can vary across jurisdictions. In Germany, for instance, there are concerns about “active” and “passive” bribery as well as the matter of bribing politicians.<sup>8</sup> In the United States, the bribery of foreign public officials by U.S. legal and natural persons in international business transactions was outlawed in 1977 with the Foreign Corrupt Practices Act. Similarly, in Europe, the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions began to change how bribery was treated in these cases. Many European countries began to amend their domestic laws to bar the payment of bribes to foreign public officials in international business transactions. Other knotty cases in this category can include an imaginary Miss X who stuffs her considerable life savings into a suitcase (as a portfolio choice) and discreetly transports the stash internationally without declaring the money as required by the authorities in both the source and destination countries. While Miss X’s life savings are proceeds of a legitimate enterprise over a lifetime, the manner in which these funds are transported violates some currency or exchange control regulation. Thus, having violated the law by not declaring the funds to authorities makes the

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<sup>8</sup> See Wolf (2006) and Peter Eigen, “How to Expose the Corrupt,” available at [www.TED.com](http://www.TED.com).

money “dirty” according to Baker’s definition. Finally, trade mispricing is an example of illegal activities that are not universally criminal but are largely aimed at evading taxes. On this point, Reuter and Truman (2004, p. 11) note that while it is tempting to claim that no taxes are paid on proceeds of unlawful activities, there are exceptions, such as when an “offender chooses to launder criminal earnings through a legitimate business and pay taxes.”

Similar to their treatment of the nature of dirty money, Reuter and Truman (2004) take a functional approach to the classification of illicit financial flows in contrast to our earlier classification of all cross-border flows (licit and illicit). Their classification is driven by the need to understand the effects of particular money-laundering controls and hence contribute meaningfully to policy choices. They identify five distinct categories subject to further consolidation depending on the purpose at hand; specifically, these are drug distribution, other “blue-collar” crime, “white-collar” crime, bribery and corruption, and terrorism. Clearly, bribery and corruption can be viewed as other “white-collar” crime, whereas terrorism can be both white-collar and blue-collar, as in cyber-attacks and physical attacks, respectively. Furthermore, as a way of highlighting the usefulness of approaching the profiling of illicit financial flows by focusing on the potential of each approach to better inform policy choices, Reuter and Truman (2004, p. 40) note that “the benefits from reducing white-collar crime by 1 percent might be seen as substantially less than those associated with a similar reduction in drug trafficking. The distribution of the benefits from reducing either of the two types of offenses may also be quite different: those who are harmed by drug trafficking are disproportionately from poor and minority urban populations, while the costs of white-collar crime are borne far more broadly across society.”<sup>9</sup> As shown in Table 2, we

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<sup>9</sup> In practice, things are not so clear-cut. For instance, the shutdown of a business due to a white-collar job can lead to severe collateral damages such as unemployment, drugs, prostitution, armed robbery, and all sorts of vices. In fact, this is the reasoning behind the “Arthur Anderson Myth” of the corporate death penalty, which we elaborate in Section 3.

derive a 5x4 typology matrix of illicit financial flows by augmenting the five crime categories delineated by these experts. These additional dimensionalities of predicate crimes, differentiated into four contingencies, comprise the extent of the reliance on cash, the scale of operations or quantities of monies involved, the severity of consequential damages, and the segment of the population most affected (e.g., the distribution of the incidence of the damages).

### **INSERT TABLE 2 HERE**

### 3. Illicit financial flows and governance

The commonly known consequences of capital flight for capital-scarce regions can be summed up as follows:

$$\textit{Resources available for development} = \textit{domestic resources} + \textit{resource inflows} - \textit{resource outflows}.$$

According to this identity, the more resource outflows, *ceteris paribus*, the fewer resources are available to be invested domestically for economic growth and development. The deeper consequences of the outflows, however, are insidious and deserving of further investigation and exposition. More formal analyses provided by Ajayi (2013), Nkurunziza (2013), and Weeks (2013) in Ajayi and Ndikumana (2014) shed fresh light on the consequences of illicit financial flows. The impact on governance is a consequence of illicit financial flows that is less known, and to which we now turn.

#### 3.1. What is governance?

We define governance as a composite of (1) structured arrangements between government and the different spheres of society and (2) institutions, including public policies, that affect

the well-being of society. Figure 1 illustrates this concept. By deliberately depicting non-state actors (NSAs) as a solid and stable triangle sitting atop of it all, we emphasize that in principle, power belongs to the people. NSAs comprise intergovernmental actors such as the World Bank, United Nations (e.g., UNODC, ECA), AfDB, ECOWAS, AU, NEPAD, and SADC; non-governmental and not-for-profit actors such as social media, academia, and charitable agencies; business actors such as the print and broadcast media, as well as banks and multinational corporations.<sup>10</sup> In Figure 1, the three societal spheres include civil society, government, and the corporate sector. A theory of the way in which these governance arrangements work is provided by institutional economists such as Douglass North (1990, 1997).

### **INSERT FIGURE 1 HERE**

According to North, “institutions are the way humans structure their interactions” (2002, p. 3). Formal rules are laws and regulations put in place by politicians who also specify how they are enforced. Informal rules are norms, conventions, and “self-imposed codes of conduct that govern much of human interaction but are also more complicated and little understood” (p. 3). North postulates that the “mixture of formal and informal rules and enforcement characteristics shape a society’s incentive structure” (p. 3). Enforcement relies on self-enforced codes of behavior, second-party enforcement or retaliatory capabilities, and government’s enforcement capacity or coercive powers. North cautions that developing norms to complement third-party enforcement mechanisms can take a very long time (over 20 years), yet if informal rules do not complement formal rules, outcomes can radically diverge from intended objectives. The informal rules are the elements that constrain behavior

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<sup>10</sup> UNODC is the United Nations Office on Drug and Crime; AU is the African Union; ECA is United Nations Economic Commission for Africa; AfDB is African Development Bank; NEPAD is the New Partnership for Africa’s Development; ECOWAS is the Economic Community for West African States; and SADC is the Southern African Development Community. For more on NSAs, see Pereira et al. (2011).

much more than the formal rules, but unfortunately society is limited in its ability to influence formal rules and enforcement (pp. 3–4).

North (1996, p. 346) argues that organizations, which arise in societies, reflect the opportunities provided by each society's institutional settings. If the institutional framework rewards kleptocracy, for example, then thieving organizations will arise. The types of political, economic, and social organizations that are spawned as people compete for survival interact with the institutions that engendered them. This interaction between organizations and related institutions in turn reshape the institutions over time in what can be viewed as a process of institutional evolution. An example is *regulatory capture*, whereby regulators are reoriented by organizations to serve the interests of those organizations rather than effectively enforce the rules and regulations constraining the behavior of those organizations. Specifically, regulatory capture is an outcome of the interaction between organizations and institutions. The concepts of interaction and institutional evolution are important in elucidating the relationship between governance and illicit financial flows.

### 3.2. The nexus of illicit financial flows and governance

Illicit financial flows are the proceeds of crime, and therefore require mapping to predicate crimes. Understanding the relationship between illicit financial flows and governance demands knowledge of the contours of the predicate crimes and the manner in which the proceeds are camouflaged. The elaborate ways and means through which the proceeds of crime are transformed to make them difficult to trace, as well as the varieties of avenues for enhancing the criminal's easy access to the clean form of the proceeds are a reflection of the opportunities provided by a country's institutional settings and thus implicates governance.

Without claiming that almost all aspects of illicit financial flows map to governance structures, we can point to credible connections between governance and predicate crimes, such as tax evasion; between governance, money laundering, and proliferation financing; and between governance and illicit financial flows in a self-reinforcing vicious circle.<sup>11</sup> We examine each of these three aspects in turn.

#### ***A. Governance and geneses of illicit financial flows: Predicate crimes***

Some proponents of ultra-free flow of funds globally (e.g. Ajilore, 2005; Collier et al., 2001; Cuddington, 1986, Deppler and Williamson, 1987) argue that such rapid movements must be viewed as strategic reactions of economic agents to the caprices of the state.<sup>12</sup> In such risky economic and political environments, a predatory state or one lacking political order can pounce on the economy by imposing controls for various reasons, including political victimizations.<sup>13</sup> These controls prevent economic agents from achieving maximal portfolio diversification benefits. Knowing that agents can anticipate its move, the state acts fast. In a chain of reciprocal expectations, foresighted agents reasoning recursively execute preemptory strikes by moving their funds even more rapidly, while others, as an anticipatory move, never keep any of their investible funds within their home country. The observable implications of such moves, in some instances, are the so-called under-invoicing of sales or parking of sales offshore, which we argue is essentially transfer mispricing. Altogether, we can envisage agents seeking out other safe alternatives, some of which are illegitimate. For example, where it is legal, dollarization allows residents to maintain Eurodollar deposits and where

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<sup>11</sup> Mindful that a theory that explains everything explains nothing, we are not attempting to claim that “fixing” governance will end illicit financial flows or that we presume to know how to fix governance.

<sup>12</sup> The biggest, most successful proponents have largely waged an ideological war. See Shaxson (2011), pp. 193-214.

<sup>13</sup> There is an alternative perspective on what is commonly labelled political victimization. Robert Bates (1981) views such a stratagem of “collective deprivation and selective benefits” as part of the repertoire of devices for disorganizing political opposition or for building support for an incumbent regime, calling it *politics of divisibility*.

prohibited, the same rational economic pursuit becomes an illegal activity. In Nigeria for example, a regulatory dispensation that allows the holding of foreign currency deposits domestically is called domiciliary accounts. Such responses by economic agents' to elements of country risk nonetheless deprive the state of seigniorage revenue. To the extent that increases in the demand for domiciliary accounts are responses to hostile investment climates, the retributions are what can be expected in a market-related economy. Other versions of the alternative narrative seeking to justify offshore havens as *laissez-faire* instruments are described in Shaxson (2011, pp. 133–214). According to this view, profligate fiscal expenditures that induce never-ending tax hikes with no tangible public benefits invite citizens to vote with their pocket by moving their money away to jurisdictions outside the reach of the state.

We do not contest views that capital movements are useful market instruments for disciplining governments on the quality of their national economic policies. When investors disagree with the direction of economic policy in a given environment, they should vote with their feet by moving their investments elsewhere; very few will disagree with this basic tenet of capitalism.<sup>14</sup> However, if capital in search of lower risk-returns is on a legitimate mission, it should have no compelling reason to be secretive or invisible, particularly given that tax avoidance is a legitimate purpose. For this reason, the growth in the scale, complexity, and ubiquity of secrecy jurisdictions worldwide require explanations beyond the legitimate goals adduced by proponents of the portfolio choice view of capital movements. *The Economist* (2013) makes a similar point with regard to the future and continued justification for offshore financial havens. Focusing on Switzerland, “still the world leader in wealth management, looking after \$2.1 trillion in assets,” the article predicts that “the next few years will provide a

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<sup>14</sup> This is the portfolio-choice argument of which there are few disagreements. See Hermes et al. (2002) and Collier et al. (2001).

stern test of the Swiss brand in private banking. They will have to show that the selling points they have long touted—political and economic stability, top-notch service, and a holistic investment approach—count for more than the ability to hide money” (p. 2).

Having acknowledged possible reasons rooted in the quality of governance that can account for illicit financial flows and their machineries, we now present in the rest of the paper an alternative narrative of the genesis of governance and illicit financial flows that makes it difficult to reconcile the portfolio choice explanation with the machinations and manifestations of illicit financial flows worldwide. We note that the genesis of drugs, organized crime, racketeering, murder, kidnapping, armed robbery, smuggling, embezzlement, cybercrimes, fraud, and even transfer mispricing may not be due directly to poor governance, even though good governance is a moderating influence. Thus, we consider these white- and blue-collar crimes as second-order linkages with governance. For this reason, we integrate their discussion into the governance-money-laundering node in section C where they are aptly featured as the underlying criminality to the proceeds being “cleaned.” Terrorism and proliferation financing will be addressed under money laundering as well, since both crimes are largely linked to global institutions and governance arrangements.

### ***B. Governance and bribery and corruption as predicate crimes***

Corruption thrives under poor governance, which provides an environment that is conducive to bribery, corruption, and other nefarious activities. Presumably, those who seek to benefit from bribery and corruption would first seek to induce poor governance if it does not already prevail. Setting up intricate schemes for successfully extracting bribes on a large scale corrodes governance and inflicts collateral damages on related institutions that normally promote economic growth and well-being. The handsome returns from this vice generate

intense struggle which largely detracts from the proper business of governance, as the battle for private control over public resources takes precedence..

The quest for power is partly explained by the fact that, in Africa as well as in many resource-rich developing countries, governments exercise near-total control over below-the-surface resources and has the ability to over-tax agricultural commodities (on-the-surface resources). Fortifying the challenge raised earlier that financial havens should prove their *raison d'être* is other than principally for nefarious purposes, the existing evidence indicates that for developing countries, there is a correlation between rich endowment in mineral resources in the context of poor governance on the one hand and illicit outflows to offshore secrecy jurisdictions on the other hand. With the exception of Ukraine, all the other resource-rich nations that are both rich in mineral resources and victims of illicit financial flows are in Africa.

Mahmood Mamdani (2011, p. 1) warns that “[t]he conditions making for external intervention[s] in Africa are growing, not diminishing.” His perception is predicated on the rising interest of global powers in Africa’s primary resources. Current estimates of the continent’s natural resource potential in oil and gas, as well as the magnitude of past spoliation, as evidenced by the magnitude of illicit flow reported in Boyce and Ndikumana (2012, pp. 19–22) suggest that the stakes are extremely high on all sides—the victims, the spoilers, and foreign interests, including offshore and onshore havens. With regard to the continent’s natural resource potential, estimates from the U.S. Energy Information Administration suggest that only 21 out of 54 African countries do not as yet show any oil and gas potential.<sup>15</sup> It would appear that the continent is replete with resources that are in high demand globally, and future resources are likely to be discovered or become

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<sup>15</sup> See US Energy Information Administration (<http://www.eia.gov>).

economically viable. Yet the continent remains impoverished. What is generally referred to as “poverty in the midst of plenty” continues to plague Africa and carries troubling implications for peace, stability, and security on the continent. Governance characterized by adherence to the rule of law is one of the most effective ways to manage this risk. Since corruption is impeding good governance and poor governance is feeding corruption—concepts that are mutually reinforcing—the chain must be broken. However, because of incessant external intervention in Africa, cutting the circular chain is not so straightforward. To do so requires a global discussion of poor governance.

Like a fish, which is said to rot from the head, the corrosive effects of grand corruption create grievous collateral damages. The costs of illicit financial flows are not just the plundered monies lost to foreign jurisdictions, but also include the lost opportunities to use these funds for local development as well as the impact on governance. Borrowing from epidemiology, we depict governance as analogous to the body’s immune system and corruption as a disease that devastates it. Weakened, the body’s defenses become vulnerable to opportunistic diseases. Whether weakened by corruption or already weak, a poor governance environment encourages opportunistic crimes, some of which gravely retard social and economic advancements. To illustrate this point, we consider two instances of grand corruption where it can be easily imagined that the direct benefit to a perpetrator like a head of state, Chief of Police or other politically exposed persons (PEPs) pales in comparison to the total economic and social costs to society.

First, consider Nigeria’s Inspectors-General of Police, Mustapha Adebayo Balogun and his successor Sunday Ehindero. Balogun, the Nigerian Police Chief from 2002–5, was jailed for six months in 2005 and fined \$30,000 following conviction for money laundering, theft, and other charges, including widespread corruption amounting to 13 billion naira or 83.2 million

dollars (in 2005 naira-US dollar exchange rate).<sup>16</sup> He spent two of the six months of his jail time as a patient in the nation's most prestigious infirmary, Abuja National Hospital, for some illness.<sup>17</sup> The whereabouts of the money recovered from Balogun is still as contentious (disagreement as to which government agency is in possession) as the amount of money actually recovered from him (Nairaland Forum, 2011). A particularly devastating aspect of Balogun's crime is its impact on institutions. The message implicit in the manner in which justice was (not) served in Balogun's high-profile corruption case is a matter of considerable consequence. The puny punishment given to Balogun for such an egregious crime, while ordinary folks who commit far lesser offenses serve harsher sentences in far worse prison conditions, is not lost on Nigerians.<sup>18</sup> As the following statement from a respected Senior Advocate of Nigeria, Femi Falana, makes clear, Balogun's case has damaged institutions incommensurably:

. . . it is now the trend to strike out or dismiss charges filed against members of the bourgeoisie. To that extent, the decision of the Supreme Court should be seen as an audacious expression of class solidarity. Perhaps, [the] majority of Nigerians are not aware of the fact that out of the over 400 convictions which the EFCC has secured in 10 years of its existence, only four members of the political class have been successfully prosecuted through dubious plea bargain deals. In the circumstance, instead of wasting meager resources allocated to the anti-graft agencies on securing convictions which are going to be set aside in favor of members of the ruling class, it is high time the Federal Government stopped charging politically exposed persons and other influential criminal suspects to court. In the atmosphere of impunity in the

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<sup>16</sup> <http://news.bbc.co.uk/2/hi/africa/4460740.stm>, Nairaland Forum (2005), and Bolaji (2012).

<sup>17</sup> For a more detailed account of Balogun's egregious crime and puny punishment, see Nairaland Forum (2006:2) Nairaland Forum(2005), Online Nigeria (2006), and Bolaji (2012).

<sup>18</sup> See the comments in Nairaland Forum (2006), Online Nigeria (2006, p. 2), and Balogun (2013, p. 3).

land, judges should equally stop the immoral practice of railroading petty criminals to jail (Balogun, 2013, pp. 2–3).

Apparently some Nigerians nowadays see anti-corruption moves by the Nigerian government as a sham perpetrated to punish and disorganize political opponents, secure the loyalty of the ruling party members, and suborn intransigents.<sup>19</sup> Sunday Ehindero, the police chief who succeeded Balogun, was on trial in 2012 for the embezzlement and misappropriation of funds donated to the police during his tenure from 2005–2007.<sup>20</sup> Using the profile of illicit financial flows represented in Table 2, it is easy to grasp the likely social consequences of crimes of this category.<sup>21</sup> When funds designed for police welfare are misappropriated, it is an assault on institutions because police is an important component of “second party enforcement” mechanisms (North, 2002, p. 3).

Second, in Peru, the Chief of Secret Police, Vladimiro Montesinos, audaciously aimed at the entire edifice of institutions and organizations that define democracy in Peru (McMillan and Zoido, 2004). Montesinos deliberately weighed all of the checks and balances in the country’s democratic structure—the opposition parties, the judiciary, and freedom of the press—that sustain democracy. He concluded that of all the instruments in the system, the most potent is free press, and set about weakening it. According to McMillan and Zoido (2004, p. 69), Montesinos paid a television station owner 100 times the payoff to a judge or a politician, and five times the aggregate amount of bribe payments to all politicians. Clearly, criminals understand the nature of the relationship between governance and the predicate crime of corruption as well as how to strategically exploit such a connection.

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<sup>19</sup>Bolaji (2013), OnlineNigeria (2006), Adebowale (2013), and BBC News Africa (2013).

<sup>20</sup> <http://www.bellanaija.com/2012/09/23/former-ig-of-police-sunday-ehindero-remanded-in-kuje-prisons-for-embezzling-n16million-misappropriating-over-n500million/>; Global Reporters Vienna (2013).

<sup>21</sup> For a poignant example of observed collateral damages from the Nigerian PEP cases, see the account in Onyeozili (2005, pp. 42-43).

### ***C. Governance, money laundering and proliferation financing***

We are careful to make the distinction between why and how one moves money in the typology of flows illustrated in Table 1. In that distinction, it is easy to appreciate that the majority of the funds, legitimate or otherwise, flow through the banking system. Even where cash smuggling obtains, those funds ultimately end up in the banking system. A challenge thus arises in reconciling the fact that such a large proportion of money laundering moves through formal channels with the statement that governments are promoters of anti-money laundering regimes. One possibility is that local financial institutions are not answerable to the laws of the states in which they conduct business, and can therefore evade national and global regulations. We submit that financial institutions can end run around effective oversight when they operate in a regime that is captive.

Looking at Table 1, hereafter referred to as matrix A for analytical expediency, it is easy to appreciate how illegitimately-acquired money can pose identification problems for banks when such money is legally transferred but the true (i.e., illegitimate) nature is unknown initially (type  $a_{12}$  in the matrix).<sup>22</sup> For this reason and others, FATF 40+9+1 recommendations exist. FATF, the Financial Action Task Force, is the standard setter for global anti-money laundering and combating the financing of terrorism (AML/CFT) regimes, particularly the preventive aspects of the mechanism. A set of 50 recommendations now includes guidelines with regard to nuclear proliferation financing and constitute the global standard as far as diligence in AML/CFT matters is concerned. FATF recommendations are important because failure to establish in-house mechanisms (at the minimum), even if those mechanisms are mere formalities, nonetheless can be probative or *prima facie* evidence of

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<sup>22</sup> For readers who may not be conversant with matrix representation, the first subscript refers to the row and the second to the column. Together those two subscripts uniquely identify a cell in a contingency table, which we call a matrix here. So the coordinate  $a_{12}$  refers to the cell 1 in the first row, second column.

total disregard for AML measures.<sup>23</sup> On the other hand, establishing and applying them indicate due diligence and can constitute a mitigating factor when a financial institution is under regulatory scrutiny or investigation for contravention.

Following “know your customer” principles or conducting due diligence can thus reduce the risk of inadvertently engaging in illicit transactions owing to identification problems of the type  $a_{12}$ . However, banks do not necessarily adhere to this sensible and ostensibly helpful course of conduct. In this regard, we cite an example involving a Swiss banking regulator and Swiss banks to show how regulatory laxity can create incentives for banks to circumvent or ignore AML rules that have been put in place to protect them and the public. In this example, the banks were ostensibly engaged in type  $a_{12}$  transactions but had not been diligent, thus creating reasonable doubts in people’s minds as to how different were the circumstances of these banks from types  $a_{21}$  and  $a_{22}$ , which are situations in which banks are deliberately or knowingly engaged in illegal transfers. In November 1999, the Swiss Federal Banking Commission (SFBC) began “investigations to ascertain whether a total of 19 banks in Switzerland had fully adhered to due diligence requirements as set out in banking law and other applicable legislation in accepting and handling funds from the entourage of the former President of Nigeria, Sani Abacha” (SFBC, 2000, p. 1). Although the majority of the banks were found wanting, there were no immediate or known direct consequences for the banks. Of the 17 banks investigated at the time of the report, 5 were fully compliant, 5 had shortcomings, and 7 were found to have made serious omissions (SFBC, 2000, pp. 6–10). In the end, none of the banks were ever sanctioned. The regulator simply expressed regrets at the violations in the expectation that banks would conduct their business with more diligence in

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<sup>23</sup> On a notorious practical application of this principle, see Reuter and Truman (2004, p. 135) on Riggs National Bank, Washington D.C.

the future.<sup>24</sup> The response of the Swiss Banking regulator to the findings of the investigation leaves open the question of whether or not the regulatory regime is captive

While the Swiss example is open to debate regarding the circumstances of a bank's involvement in the handling of illicit funds, such a benefit of doubt would be difficult to argue in egregious cases where legitimately or illegitimately acquired money is *illegally* transferred. According to our Matrix A, these would be transaction types  $a_{21}$  and  $a_{22}$ . We would like to know how such cases can continue to happen with widespread impunity. In the next section, we attempt to shed light on some known cases of outright impudence by banks.

#### ***D. The vicious circle of governance, illicit financial flows, and governance***

In many of the known or revealed cases in which banks have been major actors in money-laundering processes, the funds involved have been outflows from developing countries. According to one account, "[i]n January 2009 US law enforcement fined the British bank Lloyds TSB \$350 million after it admitted secretly channeling Iranian and Sudanese money into the American banking system. Robert Morgenthau, the Manhattan district attorney, explained how Lloyds would routinely strip out the identifying features from payments from Iran so that wire transfers would pass undetected through filters at US financial institutions" (Shaxson, 2011, pp. 249–50).

Three years after the Lloyds case, HSBC, comprised of HSBC Holdings Plc., incorporated in the UK, and HSBC Bank USA N.A., a federally chartered banking corporation headquartered in the Commonwealth of Virginia, "agreed to forfeit \$1.256 billion and enter into a deferred prosecution agreement" with the U.S. Department of Justice (DOJ) for "violations of the Bank Secrecy Act (BSA), the International Emergency Economic Powers Act (IEEPA) and

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<sup>24</sup> For a detailed account, see Swiss Federal Banking Commission (2000).

the Trading with the Enemy Act (TWEA).” HSBC admitted to anti-money laundering violations and illegally conducting transactions on behalf of customers in Cuba, Iran, Libya, Sudan, and Burma. A four-count felony charge included *willfully* failing to maintain an effective AML program, *willfully* failing to conduct due diligence on its foreign correspondent affiliates, violating IEEPA, and violating TWEA. HSBC accepted responsibility for its criminal conduct and that of its employees (see Impartial Review News, 2012 and Lowe, 2013).

Impudence is not limited to a few banks, but is so pervasive that the conduct could be considered customary practice. Such a characterization would be hardly surprising given the breadth of secrecy jurisdictions worldwide. To sustain such a high number of secrecy jurisdictions, there has to be a significant pool of brazen banks feeding the jurisdictions with the required lifeline—money. The abundance of secrecy jurisdictions can also be indicative of the global financial system’s appetite for keeping mum—*see no evil; say no evil; hear no evil*. According to a report by Global Witness (2009), it would appear that there are a bewildering number of types  $a_{12}$ ,  $a_{21}$ , and  $a_{22}$  transactions which allow banks a wide latitude for denial when accused of complicity.

. . . a raft of anti-money laundering laws [that] require them to do due diligence to identify their customer and turn down illicitly-acquired funds. But the current laws are ambiguous about how far banks must go to identify the real person behind a series of front companies and trusts. They fail to be explicit about how banks should handle natural resource revenues when they may be fuelling corruption. And if a bank has filed a report on a suspicious customer as required by the law, but then the authorities permit the transaction to go ahead, the bank can legally take dirty money. So it may

be possible for a bank to fulfil the letter of its legal obligations, yet still do business with these dubious customers (Global Witness, 2009, pp. 3–4).

Once again, we (a) see the pervasive influence of institutions as elaborated in our definition of governance and (b) confront examples of organizational conduct that reflect opportunities provided by institutional settings as predicted in North (1990, 1991). The impudence of Lloyds, HSBC, and many others such as lawyers, real estate and escrow agents, wire transfer systems, Union Bank of California, Bank of America, Citibank, PayPal, California National Bank, City National Bank, Pacific Mercantile Bank, Wachovia Bank, Commerce Bank, JP Morgan Chase, Fidelity Investments, Chevy Chase, Eagle Bank, SunTrust Bank, American University, Banco Africano de Investimentos, and Union Bank of Switzerland, to name only a few, are shaped by incentives.<sup>25</sup>

There are three noteworthy incentives shaping a trend in the global financial system towards creating colossal financial institutions that dwarf nation states. These emergent, mammoth institutions can prove to be extremely costly or impossible to regulate within individual jurisdictions. First, the existence of boundless, universal banking (product line and geographic super-latitudes) driven by advances in information communications technology and the *Internet* effectively create a supranational virtual marketplace. Second, the resulting correlations across geography and product lines which can generate unsustainable systemic risks in some circumstances can be viewed as terrorism-in-banking. For instance when regulators allow financial institutions to issue cross-default guarantees on financial instruments held by important investors, it can immunize the bank from failure as in the “too

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<sup>25</sup> For details on the duplicity of some of these players in the AML spectrum of activities, see United States Senate Permanent Committee on Investigations (2010) or earlier accounts of numerous other banks in Reuter and Truman (2004, pp. 130–36). The impudence of Riggs National Bank is notorious and needs no elaboration; also see Reuter and Truman (2004, p. 135). American University in Nigeria “accepted over \$14 million in wire transfers from unfamiliar offshore shell corporations to pay for consulting services related to development of a university in Nigeria founded by Mr. Abubakar” (United States Senate, 2010, p. 5). As the former vice president of Nigeria under the regime of Olusegun Obasanjo, Mr. Abubakar Atiku is clearly a PEP.

big to fail” doctrine. In such a circumstance, the bank basically has wired itself as a terrorist would do in order to credibly communicate its demands not to be compulsorily liquidated. More recent events which we discuss below suggest that the message being communicated indeed by banks has been understood as intended. The scale of the systemic risks envisaged marks these behemoths as “too big to fail” enterprises and “too big to prosecute” juristic persons. Three, the influence of this stratagem is already being felt in the USA and the UK in at least two ways; there may be others that we are yet to recognize, either because they are elusive, emergent, or their full implications are still evolving. In the too-big-to-fail case, we can cite the unprecedented bailout of American International Group (AIG) and big US money-center banks during the 2008 financial crisis.<sup>26</sup> For the too-big-to-prosecute case, this refers to the so-called “Arthur Anderson myth” and the recent pronouncements and steps taken by the US Attorney General, Eric Holder. The pronouncement is that Americans should come to terms with the reality that certain banks are simply too big to prosecute (Huffington Post, 2013), while the steps are in the growing use of Deferred Prosecution and Non Conviction Agreements (DPAs and NPAs), the latest instance being the HSBC case (Lowe, 2013).

Some legal scholars disagree with the conventional wisdom that “prosecuting even the largest and most established of corporations can subject them to terrible collateral consequences which risk putting them out of business, thereby causing massive social and economic harm” (FCPA, August 23<sup>rd</sup>, 2012, p. 1). Markoff finds that “the nearly indiscriminate use of DPAs with large corporations—in contrast to the DOJ’s continued tendency to prosecute and convict small companies—that predominates today is not supportable” (FCPA, August 23<sup>rd</sup>, 2012, p.1). Therefore, the two main reasons for using DPAs—the Andersen Effect and the supposed inability to gain compliance programs for structural reforms through guilty pleas—

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<sup>26</sup> Shaxson (2011) and references therein.

are largely invalid. The study recommends that prosecutors seek convictions when they can, use DPAs only when absolutely necessary, and decline to prosecute when they have a weak case that can only be successfully prosecuted by improperly pressuring the defendant. In contrast to DOJ's so-called "balanced enforcement regime," this alternative, which also can secure structural reforms, can increase deterrence of corporate crime and operate in a manner that is more transparent and more respectful of defendants' rights. As argued further by Markoff (2012, p. 44), "[s]uch a shift towards increased prosecutions and away from DPAs would both increase deterrence of corporate wrongdoing and further the interests of justice."

What is at stake are the incentive structures and their consequences. We see the DOJ as developing norms to complement the formal rules of enforcement. Judging by the interest generated, it appears that non-state actors are equally apprehensive of the significance of the emerging norms (of DPAs and NPAs) as a form of institutional change. Mammoth economic organizations are reshaping institutions and institutions in turn appear to be bending to the forces unleashed by these organizations. Unfettered by regulations, ethical considerations, or political accountability, global financial organizations such as HSBC, AIG, and JP Morgan are becoming more powerful than national governments because, unlike national governments, they are not socially and politically held accountable. The confluence of politics and money makes economic organizations even more influential than they need be, given that they are not politically accountable entities.<sup>27</sup> The centrality of governance to the business of illicit financial flows appears to be well accepted. We have so far attempted to elaborate that interface and thereby find lessons that can inform strategies to curb illicit financial flows. We turn to this aspect in the concluding section.

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<sup>27</sup> For readers still harboring any doubts about the corrupting influence of corporations on politics, consult a brief on the Enron collapse by Puscas (2002). Additionally, see the documentary on the musical chairs between Washington and Wall Street in *Inside Job* (2010), directed by Charles Ferguson. Similarly, as has been noted in Shaxson (2011, pp. 247–9), the City of London is corporate influence in the world's foremost financial center personified. Lord (2013) draws a parallel between two similar incidents of corporate influence in the 1980s and 2013.

#### 4. Conclusions and recommendations

Grand corruption is at the core of the nexus of governance and illicit financial flows. It corrodes governance, which in turn engenders opportunistic crimes. These crimes fester and fuel the rot that grand corruption engenders. Moreover, the consequences of grand corruption are multidimensional. First, it is a very profitable predicate crime. Second, it stops other rules from being enforced lest those interfere with the business of grand corruption. Cognizant that formal rules are put in place by politicians who specify how they are enforced, we conclude that, in forcing politicians to turn a blind eye to certain kinds of enforcement because those may disturb corruption, grand corruption implicitly destroys “institutions as investment” in growth and development.<sup>28</sup>

We can further conclude from the analysis developed in this paper that there are at least two likely antagonistic circles in the illicit flow process—a virtuous circle and a vicious circle—both rooted in one common factor, namely, the strategic complementarity between corruption and governance. In the virtuous cycle, good governance curbs corruption. In the vicious cycle, corruption corrodes governance because poor governance enables corruption. In considering the implications of these opposing circles, suggesting that good governance fix corruption, where good governance does not already obtain, only begs the issue. The vicious circle cannot be displaced by the virtuous circle because they exist in parallel, but opposing orbits. Thus, they can be considered multiple equilibria. If society happens to land in either of these states, such a state can endure or self-perpetuate unless a conscious and sustained effort is made to change the situation. The desired change will not happen spontaneously.

Going forward, the idea that civil society has the power and duty to displace the vicious circle irrespective of the nature of the political regime is a topic for further research. In a

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<sup>28</sup> For more on institutions as investment in development, see Bates (2006) .

democracy, civil society can and should deliver the required efforts by creating the right incentives for politicians to care about the consequences of illicit financial flows. The cognoscenti call this prerequisite *political will*. But we should emphasize, however, that politicians do not create political will. They respond to it. It is the governed or those who consent to be governed who should align the political fortunes of the policymakers to the consequences of illicit financial flows. All forms of government crave legitimacy. Even in a dictatorship, the duty of conferring legitimacy on the regime rests with civil society.

Further research on how to enable and sustain a habit of political participation promises to be a useful agenda for all nations, developed and developing, democratic or otherwise. Civics used to be on the curriculum and was actually taught as early as primary school. Like the fate of ethics in business school curricula until its re-emergence after the Enron and Arthur Anderson fiascos and other corporate governance scandals in 2002, the study of civics seems to have become relegated to the past.<sup>29</sup> If global governance architecture encourages banks to “do the crime, pay the fine, and do no time,” then the observed, rampant impudence of banks would be understandable and we would not be surprised should banks increasingly resemble a police establishment run by ex-convicts. Curbing illicit financial flows in such a circumstance would be far-fetched; it is already proving to be a daunting task as the US Attorney General Eric Holder enunciated. Civil society therefore must live up to its responsibilities.

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<sup>29</sup> Leonce Ndikumana offers this interesting perspective on the demise of civics in schools. One of the reasons why civics education has disappeared from school curricula is that past regimes used it as a propaganda machine, an indoctrination medium, rather than instruction in morality and citizenship. Thus it succumbed during political regime transitions.

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**Table 1: Typology of Financial Flows**

<b>Why one moves money (Provenance)</b>   <i>How one moves money (Type of transfers)</i>	<b>Legitimately acquired</b>	<b>Illegitimately acquired</b>
<i>Legally transferred</i> 	Good Money	Dirty Money
<i>Illegally transferred</i>	Dirty Money	Dirty Money

Source: Authors' rendition based on a collection of definitions in Dev Kar (2011), Reuter and Truman (2004), and Baker (2005).

Note: Illegitimately acquired money may be known or unknown. For instance, stolen money (illegitimately acquired) can be legally transferred if the true nature or origin of the money is not known or remains unknown.

**Table 2: Matrix of dimensionality of illicit financial flows**

<b>Crime features</b>  <b>Crime categories</b>	<b>Cash Intensity</b>	<b>Scale of operations or magnitude of the flows</b>	<b>Severity of damages</b>	<b>Incidence of damages</b>
<b>Drugs</b>	Very high	Global	Extreme	Pervasive
<b>Other blue-collar crimes</b>	Depends on specifics	Depends on specifics	Depends on specifics	Depends on specifics
<b>Other white-collar crimes</b>	Depends on specifics	Depends on specifics	Depends on specifics	Depends on specifics; e.g., Arthur Anderson, Enron, and the recent global financial crisis illustrates the complex manifolds
<b>Bribery and Corruption</b>	Depends on specifics	Highly variable	Variable; can be extreme	Pervasive
<b>Terrorism and Proliferation financing</b>	Depends on specifics	Variable	Extreme	Pervasive

Source: Authors' rendition based on Financial Action Task Force (FATF) typologies & Reuter and Truman (2004).

Note: This matrix portrays the dimensionality of illicit flows and hence the social and policy complexity of the problem. In principle, each of these cells can be populated with jurisdiction-specific data. It would not be unreasonable to expect the United Nations Office on Drug and Crime as well as Interpol to aspire to attaining the capacity to provide such a data set.

**Figure 1: Governance Arrangements**



Source: Authors' conceptualization. Composition of non-state actors (NSAs) is drawn from Pereira et al. (2011).