Research reveals serious issues with Australia's AML/CTF ratings

With another 7 new reports released on 20 September, at least 18 countries' AML/CTF regimes have been up-graded since Australia's 2015 assessment, yet Australia's reputation continues to be tarnished by 'effectiveness' ratings with major flaws, according to independent research.

But, Australia is no exception. Although the Paris-based Financial Action Task Force regards 'effectiveness' ratings the "main component", none of the re-ratings since the new rules became operational in 2014 re-examined the 11 'effectiveness' measures. Of 52 countries assessed for effectiveness, reassessments have only looked at less important 'technical compliance' measures.

This means that, without its own update, Australia's reputation continues to be affected by its 'effectiveness' ratings from over three years ago, which the latest research published in the *Journal of Money Laundering Control* finds doesn't properly evaluate effectiveness. (Australia was awarded only one 'high' rating, and lowly 'moderate' ratings in 6 of 11 'outcome' measures).

New criteria seek to assess effectiveness

FATF introduced a new 'effectiveness' methodology in 2013 because compliance with its "40 recommendations" (previously the sole focus of evaluations since 1990) gave no assurance that money laundering regulations were effective.

An extensive process demanding significant resources and preparation by authorities, evaluations now assess anti-money laundering regimes based on two sets of rules: technical compliance with FATF's 40 recommendations, and 'effectiveness' based on 11 'outcome' measures. But the new study reveals major flaws with the effectiveness criteria.

Measuring effort, not outcomes

According to the study's author, Dr Ron Pol from international consultancy AMLassurance.com (whose PhD thesis at Griffith University found new ways to access and assess evidence of lawyers, accountants and real estate agents enabling criminal transactions), "misapplication of outcome labels for what are, in truth, simplistic *output* and *activity* measures miss an opportunity to evaluate the real impact of anti-money laundering rules."

He says that FATF's new methodology doesn't evaluate outcomes in the sense generally understood as the effect or impact of regulations. "More meaningful outcome measures, for example, might include the extent to which the system better allows authorities to reduce and prevent crime, and to cut the social and economic harms caused by serious crime like drugs-trafficking, corruption, fraud and tax evasion. Some of those measures are difficult to evaluate" says Pol, "but assessing anti-money laundering regimes by superficial 'easy-to-measure' metrics suggests that the intensive rating exercise conveys value more as a rhetorical device than any real measure of effectiveness."

"That's because the current measures largely reflect the efforts of regulatory and enforcement authorities, not whether those efforts have any meaningful impact on serious crime."

'Tick-box' compliance extended

"Moreover", adds Pol, "assessors often use the same evidence to assess both the old and new criteria. But, compressing FATF's 40 recommendations into an abbreviated yet broadly equivalent list of so-called 'outcomes' adds little new evaluative capability beyond 11 more boxes to tick."

"The nature of any tick-box system means that it's possible for jurisdictions to get high ratings without much impact on crime, and vice versa" says Pol. "To their credit, authorities appear often to have focused more on crime prevention than better ratings, although close examination of more than 50 evaluations to date reveal ways to achieve both. Nonetheless, although the new ratings system arguably lacks much meaning, low scores have a very real impact on any jurisdiction's access to financial markets."

Effectiveness gap evidence mounting

Another academic paper also notes "enormous" frustration that, despite nearly 30 years of money laundering obligations (now imposed on millions of firms in nearly 200 countries) the "huge and growing cost of compliance has been accompanied by little observable effect". Professors Levi, Reuter and Halliday say that the modern anti-money laundering system is "highly cost-inefficient" and has failed "to produce credible evidence of [its] effectiveness."

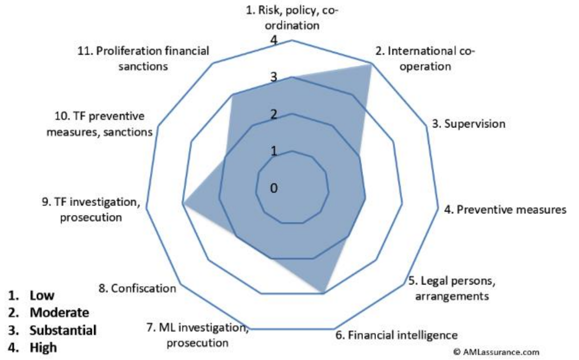
The new study's detailed analysis makes similar findings. It concludes that FATF's new methodology offers few reliable indicators about the effectiveness of money laundering controls.

Positive signs

But the new study ends optimistically. "FATF's frank acknowledgement that evaluating for effectiveness was missing, and important, is a positive step", says Pol. "Likewise, that outcomes matter. FATF also frequently adjusts its standards and guidance as circumstances change. If it accepts that some principles and practices underpinning its effectiveness framework might be improved, that tradition might reasonably be expected to continue."

Additional notes

FATF effectiveness ratings: Australia



This chart (and other countries assessed) is available in PPTX and PDF formats.

Data source: FATF/APG Mutual Evaluation Report: Australia (April 2015): here, pp12-17

About the Financial Action Task Force

- About FATF & APG
- About mutual evaluations: here
- About FATF 'effectiveness': here
- About FATF's 'effectiveness' methodology: here ('immediate outcomes' on p16 & ratings on p21)

Supplementary material: Australia

The new study used 'immediate outcome 7' (money laundering investigations and prosecutions) to illustrate differences between *outputs* and *outcomes*, and why it matters.

Australia received a 'moderate' rating on this measure, defined as achieved only "to some extent", with "major improvements needed".

Assessors recognised that Australia's main objective is to disrupt and deter serious profit-motivated crime such as drugs trafficking, noting that prosecutors didn't focus much on money laundering charges. Assessors suggested that police should 'double charge' offenders for money laundering as well as the primary offence. It should then be "relatively easy" for Australia to achieve a higher rating.

"But," says Pol, "more money laundering prosecutions (an *activity* or *output* measure) might, or might not, help achieve the (crime prevention) *outcomes* that authorities seek."

The study gave a hypothetical example where law enforcement agencies detect and prosecute twice as much serious crime but, with prosecutors overwhelmed, no money laundering charges are laid. Authorities would of course promote their doubling of crime detection to influence ratings, but with fewer money laundering cases than the low number already bemoaned by assessors, Australia's FATF 'effectiveness' rating might fall even further.

"Bizarrely", says Pol "the prospect of *lower* 'effectiveness' ratings if authorities successfully disrupt *more* serious crime is an unintended consequence of focusing on simple output measures rather than crime prevention outcomes. Presumably, that would not be the intention of Australian authorities, or FATF."

1. **The full study**: Pol, R, F., *Anti-money laundering effectiveness: Assessing outcomes or ticking boxes?* Journal of Money Laundering Control (2018), Vol 21 No 2: http://dx.doi.org/10.1108/JMLC-07-2017-0029. About *Journal of Money Laundering Control*: here

2. **Companion study**: Pol, R. F., *Uncomfortable truths? ML=BS and AML=BS²*, Journal of Financial Crime (2018), Vol 25 No 2: http://doi.org/10.1108/JFC-08-2017-0071. About *the Journal of Financial Crime* here.

3. **Other study referenced**. Levi, M., Reuter, P., Halliday, T., *Can the AML system be evaluated without better data?* Crime, Law and Social Change (2017), available here

4. **Acknowledgements**. An earlier version of the analysis which formed this article (in the author's PhD thesis) was reviewed by supervising Professors Jason Sharman (now at Cambridge) and AJ Brown and Duncan McDonnell (Griffith), and examined by Professors Michael Levi (Cardiff) and Louis de Koker (La Trobe), before the *Journal of Money Laundering Control's* own peer-review process. The author is grateful for their invaluable assistance. Any errors are the author's alone.

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The study's author is a political scientist linking public policy with effectiveness. This involves examining not only whether rules exist, or meet recognised standards, or countries adopt them, or even if firms comply with them, but whether they work. Do they produce intended outcomes? Also: 1-page outcome effectiveness & AML/CFT effectiveness profiles.	Tel: +64 (4) 566 5144 Mobile: +64 (27) 241 1163 Email: Ronald.Pol@TeamFactors.com, or Ronald.Pol@AMLassurance.com