

## Study reveals issues with Latvia's low anti-money laundering ratings

Findings in a leading peer-reviewed journal call into question the evaluation of Latvia's anti-money laundering regime, released on 23 August 2018.

The European anti-money laundering watchdog MONEYVAL awarded Latvia lowly 'moderate' ratings on eight measures, and the lowest possible rating for another two of 11 areas assessed for 'effectiveness'. But the new research finds new global assessment criteria do not properly evaluate the effectiveness of anti-money laundering regimes.

### New criteria seek to assess effectiveness

The Paris-based Financial Action Task Force 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, "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 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 countries' 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 is because the current measures largely reflect the efforts of regulatory and enforcement authorities, not whether those efforts have any meaningful effect or 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 focus 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."

The impact of perceptions, by ratings or other public pronouncements, is real. In February, for example, simply issuing a draft notice that it intended to ban US correspondent banking relationships with ABLV for alleged money laundering breaches, the [US Treasury in effect closed Latvia's third largest bank](#). Six months' later, Latvia was still "[struggling to regain access to the US dollar market](#)".

### 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.

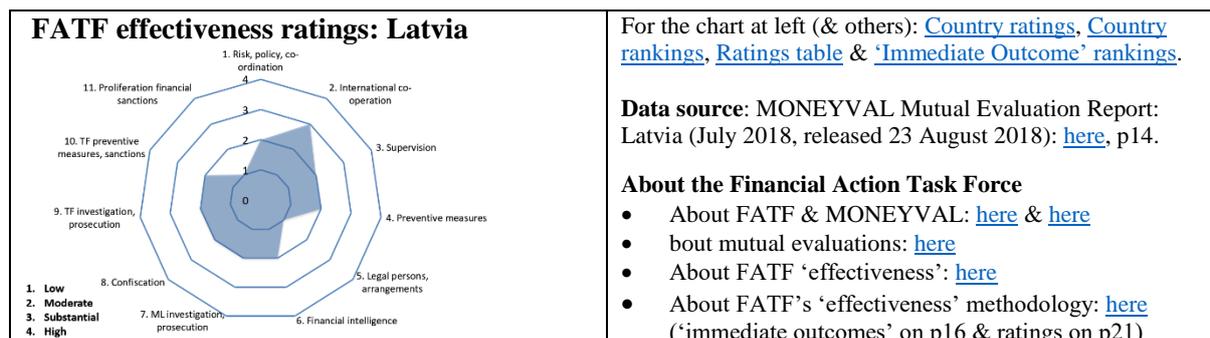
### Positive signs

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."

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[Additional detail about Latvia's assessment below]

## Additional notes



### Supplementary material: Latvia

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

Assessors noted that Latvia has “a sound legal system” and “the capacity to investigate and prosecute money laundering and associated predicate offences”. Authorities have “adopted a number of action plans to combat organised crime and the shadow economy”, but “none of them is specifically devoted for identifying or prioritising money laundering” said assessors. Instead, Latvian authorities focus “predominantly on the predicate offences”, such as drugs trafficking, fraud and other organised crime. Assessors’ decried the “modest” number of money laundering convictions “compared with the high number of convictions for predicate offences in the same period”, and concluding that “major improvements” were needed, awarding a lowly ‘moderate’ rating for this measure.

Clearly, more money laundering prosecutions would help boost the country’s ‘effectiveness’ 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.” He gave a hypothetical example where enforcement agencies detect and prosecute twice as much serious crime but, with prosecutors overwhelmed, and consistent with Latvia’s focus on the underlying crime, no money laundering charges are laid.

Authorities would of course promote their doubling of crime detection to positively influence ratings, but with no money laundering cases, Latvia’s FATF ‘effectiveness’ score on this measure might conceivably remain low.

“Bizarrely”, says Pol “the prospect of the lowest possible rating if authorities successfully disrupt significantly *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 Latvian 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=BS<sup>2</sup>*, 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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