Research reveals serious issues with AML/CFT assessments as Pacific nations re-rated, and NZ prepares for 2020

In reports issued late last week, the anti-money laundering regimes of Fiji, Samoa and Vanuatu were upgraded on 'technical compliance' ratings. But their reputations and access to global markets remain tarnished by 'effectiveness' ratings that contain major flaws, according to independent research.

Although it re-rated 40 'technical compliance' metrics, the Asia-Pacific money laundering watchdog didn't upgrade 11 'effectiveness' measures which the Paris-based Financial Action Task Force considers the "main component" of such evaluations.

Each country therefore continues to be judged based on ratings that, according to research in the latest edition of the *Journal of Money Laundering Control*, doesn't properly evaluate effectiveness: "Anti-money laundering effectiveness: Assessing outcomes or ticking boxes?"

New Zealand is due to be assessed on both 'technical compliance' and 'effectiveness' standards in 2020.

New criteria sought 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. But the research study reveals major flaws with the new effectiveness criteria.

Measuring effort, not outcomes
According to the study's author, Dr Ron Pol from Wellington-based 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 cuts the social and economic harms caused by serious crime like drugs-trafficking, 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" industry frustration that, despite nearly 30 years of money laundering controls, the "huge and growing cost of compliance has been accompanied by little observable effect" ("Can the AML system be evaluated without better data?"). 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.

A companion study in the *Journal of Financial Crime* ("Uncomfortable truths? ML=BS and AML=BS^2") also reveals that the modern anti-money laundering system, in every country assessed (including New Zealand, and globally) is "almost completely ineffective", with barely the impact of a rounding error on criminal accounts.

Positive signs
But the new studies end 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."

Supplementary material

More details for each of the 7 APAC countries' AML/CFT regime re-ratings:
Thailand, Sri Lanka, Fiji, Samoa, Vanuatu, Bangladesh & Bhutan.

AML/CFT 'effectiveness' ratings, compared
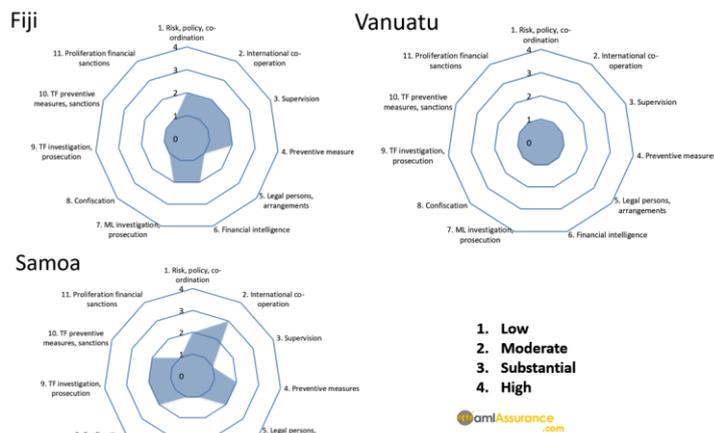
Charts for all the 52 countries assessed to date for AML/CFT 'effectiveness'
- FATF 'effectiveness' country ratings (PDF) & PPT format
- FATF 'effectiveness' country rankings
- FATF 'effectiveness' ratings table
- FATF 'outcome' rankings

Peer-reviewed journal articles on AML effectiveness
- Pol, R F, Uncomfortable truths? ML=BS and AML=BS[2], *Journal of Financial Crime* (2018), Vol 25 No 2. About the journal here. Testing a core pillar underpinning the AML/CFT narrative. Is it effective?

- Pol, R F, Anti-money laundering effectiveness: Assessing outcomes or ticking boxes? *Journal of Money Laundering Control* (2018), Vol 21 No 2. About the journal here. The first independent assessment of the global method for evaluating countries' AML/CFT 'effectiveness'. Does it work?

- Levi, M, Reuter, P, Halliday, T, Can the AML system be evaluated without better data? *Crime, Law and Social Change* (2017), Vol 69 No 2.

Methodology for the above charts
- Pol, R F, Anti-money laundering effectiveness ratings: Ranking countries and outcomes, *ACAMS Today*, Dec 2017-Feb 2018. The first independent ranking of countries' AML/CFT 'effectiveness' ratings [paywall] [free summary here]

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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