

# Seeing GFI's report on illicit financial flows in 2006-2015 through three Marys' eyes

Alex Erskine<sup>1</sup>, 10 February 2019

Global Financial Integrity (GFI) has updated its flagship annual 10-year report providing its estimates of illicit financial flows for developing countries<sup>2</sup>. It is GFI's 8<sup>th</sup> (or 9<sup>th</sup> – there were two in 2011) such effort. The period under review has now rolled on to 2006-2015.

Since its publication in January media reports in some countries have mostly highlighted GFI-estimated illicit outflows. But this time perhaps overall there has been less follow-up, which may be a good thing<sup>3</sup>. This critical note – imagine it's penned by the first of the Marys, Mary I (**Mary, Mary Quite Contrary, Bloody Mary**) – may explain why. It finds GFI's series cluttered and adrift, but it could be improved.

## Marie Kondo, queen of de-cluttering, has had only a minor influence on GFI's report

Marie Kondo<sup>4</sup>, the second Mary, apparently sets 7 *KonMari* tasks: 1. Tidy all at once; 2. Visualise your destination; 3. Identify why you want to live the way you envision; 4. Determine if each item “sparks joy”; 5. Tidy by category, not location; 6. Tidy in the right order; and 7. Discard before you put things back.

Marie Kondo says tidiness promotes world peace. GFI has not been paying her enough attention.

1. Rather than **tidy all at once**, GFI has progressed iteratively, each year making many seemingly minor changes. Their complexity mean comparisons of GFI estimates over time are impossible.
2. At the start GFI did **visualise a destination** but it seems to have lost its way. The latest report has no “quotable quote” about illicit funds “draining development”, for the compelling reason that GFI's main estimates of illicit financial flows **from** developing countries **into** advanced countries are **less** than its estimates of illicit financial flows **into** developing countries **from** advanced countries, not just in 2015 but in most years since 2010<sup>5</sup>.
3. Similarly in this report GFI seems to have lost **clarity about its purpose**. GFI's promo for the report deceptively boasts the IMF, OECD, UN and World Bank use GFI's definition of illicit financial flows, but notably omits to say they reject the way GFI makes its estimates. The report itself is crammed with complexity but does not seek to win the more important battle of persuading sceptical readers that its estimates have any meaning. No one would want to live in that way.
4. What evidently does give GFI **a spark of joy** are mismatches found in trade databases. This is the 8<sup>th</sup>/9<sup>th</sup> update that is based around GFI's 'mirror' trade data mismatch estimates (which it then calls trade misinvoicing) using the IMF DOTS database. Such a spark of joy that GFI has now added a second set of estimates made using the UN Comtrade database. The estimates are different, raising questions over the credibility of either set of estimates. Marie K would see more clutter.

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<sup>2</sup> GFI 2019. <https://www.gfintegrity.org/report/2019-iff-update/>

<sup>3</sup> See Forstater 2016 and Erskine 2018.

<sup>4</sup> Kondo 2011 and Northrup 2018.

<sup>5</sup> GFI characterises illicit inflows as likely associated with tax fiddles, not funds available for development.

5. GFI has defied *Kondo-san* in this report by **tidying by location** (i.e. the report) **rather than by category** (i.e. the type of estimates). It has shortened the report to 56 pages, less than half the original report. But too much that previously was thought to matter has been dumped or changed without explanation. What GFI used to call “Total Illicit Financial Flows” is now described as “Estimated Potential Trade-Related Illicit Financial Flows”. So, are there now **non-trade-related** illicit flows that are not included?<sup>6</sup> And GFI has further demoted the mismatch in the balance of payments that is “net errors and omissions” (NE&O, or in GFI jargon ‘unrecorded BoP flows’), which used to be one of GFI’s two components of its estimate of total illicit financial flows. Now it is only an addendum in the summary table, ensuring GFI’s full estimates are dominated by its estimates of trade data mismatches.
6. Rather than **tidy in the right order** (addressing the much-criticised GFI assertion that mismatches in ‘mirror’ trade databases are almost always due to intentional criminal behaviour intended to spirit monies illicitly across borders), GFI has instead doubled down, creating a second set of database mismatches. And GFI adjusts the mismatches found in the second database for some factors likely to distort the numbers (e.g. for countries that are landlocked versus coastal) but does not carry this adjustment over into its primary set of estimates.
7. Such untidiness shows GFI has ignored the Kondo imperative to **discard rather than place things back** (e.g. persisting with its insistence that trade database mismatches show criminal intentions). GFI 2019 incorporates some sensible World Customs Organisation recommendations<sup>7</sup>. But it ignores a key finding in that WCO report that “up to 85% [of GFI-type trade data discrepancies] were explained by the different attribution of trade partners (due to transit or indirect trade), trade recording system (Customs free zone), CIF/FOB valuation, time-lag, currency conversion, confidential trade, etc.”<sup>8</sup>. “Up to 85%”! Marie Kondo would urge GFI to discard trade misinvoicing and GFI’s own ongoing weekly briefings on Transnational Crimes would support that move<sup>9</sup>.

### **Mary Celeste, the third Mary, may explain more than Marie Kondo**

It is unclear where is GFI heading with these rolling annual updates. They consume a lot of resources on the part of both authors and readers which could be more usefully employed. This series now has all the appearance of the *Mary Celeste*, adrift and ever more mysterious. Sightings now and in future risk continuing to distract from the research needed to advance the illicit financial flows agenda.

The estimates in the report should be seen for what they are: trade database inaccuracies. Given the size and persistence of mismatches in spite of some ongoing database quality improvements (e.g. including this year an overdue narrowing of the c.i.f.-f.o.b. differential and falling transport margins), GFI could usefully recommend further improvements in the databases that would narrow the mismatches.

### **Final three-Mary advice**

Mary Contrary’s advice for GFI’s next annual update: more Marie Kondo and less *Mary Celeste*; or off with their heads! Such “life-changing magic” would benefit readers and help curb illicit financial flows.

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<sup>6</sup> Following the logic underlying GFI’s long-held assumptions, non-trade-related illicit financial flows would be incorporated in “unrecorded BoP flows”, i.e. the net errors and omissions term in the balance of payments.

<sup>7</sup> See World Customs Organisation 2018.

<sup>8</sup> See Yeon Soo Choi, Etim Ibok and Frank Kalizinje, Chapter 7 in World Customs Organisation 2018.

<sup>9</sup> See GFI. Ongoing.

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