# Introducing the Financial Secrecy Index

*The Financial Secrecy Index begins a new phase in global understandings of financial secrecy, illicit financial flows and corruption. It brings into focus, for the first time, the global infrastructure of secrecy jurisdictions which encourage and facilitate illicit financial flows.*

## Shining light into dark places

The World Bank's Stolen Asset Recovery (StAR) initiative in June 2007 endorsed estimates that illicit financial flows across borders added up to $1-1.6 *trillion* per year, about half of it leaving developing and transitional economies. More recent estimates put the figure of illicit financial flows out of developing countries alone at around $800 billion - $1.06 trillion. Looking at a related issue, the Tax Justice Network recently estimated, conservatively, that about $250 billion is being lost in taxes each year by governments worldwide, as a result of wealthy individuals holding their assets offshore. Christian Aid also estimates that illegal tax evasion by international business alone deprives developing countries of US$160 billion in tax revenues each year. Clearly, aid flows from rich countries of around US$100 billion a year are relatively insignificant when compared to the massive illicit financial flows and tax losses incurred by poorer countries.

These staggering sums are encouraged and enabled by one common element: secrecy in international finance. Jurisdictions are increasingly competing to offer ever greater forms of secrecy, so as to attract dirty money of all kinds, and a global industry has grown up to promote, facilitate and service these deadly flows.

As if this weren't bad enough, secrecy in international finance has many other harmful effects. It distorts trade and investment flows, and creates a criminogenic environment for a litany of evils that hurt the citizens of rich and poor countries alike: tax evasion, fraud, insider-dealing, embezzlement, non-payment of alimony, money laundering, evasion of prudential banking regulations, and much more besides.

Planet Earth, we have a problem.

## Who are the true culprits?

The Financial Secrecy Index (FSI) focuses on 60 secrecy jurisdictions, a term we prefer to the more commonly used *tax haven*. These places offer not only freedom from tax, but also a shield against any number of rules, laws and regulations of other jurisdictions. What these places have in common is legal and financial secrecy.

Numerous databases and indices exist to help identify corruption and other governance problems *within* countries. Yet because secrecy jurisdictions always facilitate activities carried out *elsewhere,* this is their core business, it serves little or no purpose to focus merely on what happens inside individual jurisdictions. Financial secrecy must be analysed on a global level.

 

Until now there has been no way of identifying and ranking the darkest and most dangerous corners of international finance. The FSI reveals for the first time which jurisdictions are most to blame for supplying financial secrecy, and provides new pointers for global action.

The FSI combines two measurements, one qualitative and one quantitative. The qualitative measure looks at a jurisdiction's laws and regulations, international treaties, and so on, to assess how secretive it is. The assessment is given in the form of an opacity score. The higher the score, the more opaque the jurisdiction. The second quantitative measurement attaches a weighting to take account of the jurisdiction's size and overall importance to the global financial markets. Details on the methodology are available here [ADD LINK].

## What is the significance of this new index?

For too long, governments and campaigners have focused almost exclusively on narrow problems, ignoring the bigger picture. For example there has been a heavy focus on terrorist financing, and on narrowly defined categories of money laundering. But the far larger problems of tax evasion and abusive trade mispricing, for example, have received much less attention, notwithstanding some timid recent pushes on tax evasion from the G-20 countries and the Organisation for Economic Cooperation and Development (OECD) [1]. Yet these far larger problems operate through, and perpetuate, exactly the same mechanisms of offshore financial secrecy that facilitate cross-border flows of terrorist and drug financing. Tackling one, whilst ignoring the other, is folly.

The only realistic way to address all these problems successfully is to tackle them at root: offshore secrecy and the global infrastructure that creates it. A new index ranking the jurisdictions most responsible for providing financial secrecy is therefore essential. The FSI is that new index.

As well as identifying the providers of financial secrecy, the FSI will help open up entirely new areas of debate and analysis. Three examples help illustrate this.

**Secrecy**

For decades it has been popularly believed that bank secrecy – such as that offered by Austria, Luxembourg and Switzerland – is the touchstone of offshore financial secrecy. This is a myth. Bank secrecy is important, to be sure, but a range of predominantly Anglo-Saxon jurisdictions use other mechanisms towards the same end. Trusts, for example, or certain kinds of anonymous companies offered by places like Delaware in the United States, are used to disguise true identities and ownerships in far more devious and effective ways than through bank secrecy alone. The FTI helps bring into focus jurisdictions such as Delaware and the Cayman Islands that specialise in these kinds of subterfuges, as well as those like Switzerland and Luxembourg that rely more on pure bank secrecy.

[1] The OECD's evolving "blacklist" initiated after the April 2009 G20 meeting, and which has been widely touted, is more of a whitewash than a blacklist. This page [LINK] shows why the OECD's method is unacceptable, and this Tax Justice Network briefing paper here describes better approaches.

 

**Corruption.**
In the field of international governance and transparency, the most famous ranking of corruption is Transparency International's *Corruption Perceptions Index* (CPI.) To a large extent the CPI is focused on bribe-taking in the public sector. The CPI ranks poor countries in Africa and elsewhere – predominantly the *victims* of the estimated $800 billion- $1.1 trillion in annual illicit financial flows – as the "most corrupt", while many of the jurisdictions *receiving* these flows of dirty money (Switzerland, Singapore, the United Kingdom, Luxembourg, and so on) can pride themselves as being amongst the "least corrupt." Clearly, a fuller picture of corruption is required.

To illustrate the problem, consider the following. Businesses looking to invest overseas find it useful to know that Nigeria, say, is ranked among the world's most corrupt nations. But this is of little help to ordinary Nigerians, who want to know considerably more: *where* their money is going, *how* it is leaving, and *who* is helping it leave. The brutal Nigerian dictator Sani Abacha raked billions of dollars of Nigeria's oil wealth into his personal accounts before he died. But *where* were those accounts? *Who* helped him move his money out of Nigeria and into new accounts? *Which* jurisdictions did the money pass through and eventually settle in? Abacha represented the demand side of corruption. London, Zurich and other centres of international financial secrecy provided the supply side.

The FSI ranks, for the first time, which jurisdictions are most responsible for the "supply side" of corruption. It provides a basis for a new wave of understandings about corruption and the phenomena of illicit financial flows.

**Market Integrity**
Fair international trade has the potential to generate enormous economic growth and spread benefits across global society – but it has often not worked out that way. Secrecy is one of the most important reasons why markets have not worked as well as they should, for the developing world in particular.

Secrecy prevents the free flow of information, stopping investors from making the best-possible decisions and utilising resources most efficiently. Secrecy also severely distorts markets by shifting investments and financial flows not to where they will be most productive, but to where they can acquire the greatest benefits of secrecy. For example, the availability of financial secrecy encourages companies to create complex and opaque offshore structures for purposes of tax avoidance and evasion. This complexity hinders effective regulation and obscures where risks might be lying within an organisation. By identifying the providers of secrecy, the FSI turns the spotlight on the jurisdictions which prevent international trade from benefitting the poorest people on Earth.

## An analysis and an invitation

Ultimately the FSI is both an analysis and an invitation. The analysis is entirely original. The invitation is for civil society groups, politicians, corporations, academics, and others to acknowledge the problem of global financial secrecy and illicit finance, and to take action against them.

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