The Economic Effects of Money Laundering on the Nigerian Economy: Some Emerging Issues

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Although the economic effects of money laundering on economic development are difficult to quantify, it is evident that such activity damages the financial institutions which are critical to economic growth. Besides, it reduces productivity in the economy's real sector by diverting resources and encouraging crime and corruption, which slow economic growth. Furthermore, such activity can distort an economy's external sector through international trade and capital flows to the detriment of long-term economic development. This paper attempts to explore the economic effects of this malaise on the Nigerian economy. It observes that if money laundering is not tamed, it has the potential of propagating banking system distress, capital flight and exchange rate misalignment. The paper, therefore, calls for a technologically driven regulatory framework, reforms of the existing law of evidence to tackle electronic dimension of money laundering and domestic forfeiture laws, the hastening of e-banking and electronic payments system and, finally, a need for global cooperation in implementing money laundering laws and jurisdictional issues.

Keywords: Money laundering, criminalization, corruption, placement, layering, integration, reputational risks, reputational effects, Inward and Outbound flows, e-banking.

JEL Classification Numbers: K42

I. Introduction

Money laundering has assumed a phenomenal growth the world over and, there is a renewed thinking that money stinks. This shift from the erstwhile view that ***"pecunia non olet"***, meaning that money does not stink, has provided the impetus to launder it

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by ensuring that money is used without identifying the source and hence, forestall any danger of confiscation. Money laundering is facilitated through the co-operation of third parties whose role frustrates the detection and subsequent application of appropriate sanctions. The criminalization of money laundering is aimed at disrupting the co-operation provided by third persons in hiding the proceeds from crime and giving the proceeds a legitimate appearance.

Globally, tbe fight against money laundering has been fierce against the backdrop of the attendant consequences associated with this type of crime. As the world is experiencing economic globalization, economic crimes have also been globalized, and its ***modus operandi*** have become even more sophisticated.

Economic crimes do not only harm individuals, but also sometimes cause great loss to public property, and could result in the damaging of investors' confidence in doing business in a particular country, leading them to invest elsewhere. Thus, economic crimes may ultimately undermine the basis for sound socio-economic development in a country. Nigeria's recognition of the importance of the fight against economic and financial crime is hinged on its economic consequences on the economy.

Thus, this paper examines the economic effects of money laundering on the Nigerian economy. It also identifies the trend, transitory and cyclical patterns in the net foreign assets of the deposit money banks (DMBs) in the country in order to put into perspective the widespread use of DMBs as channel for money laundering activities. The paper, in addition, reviews the efforts at combating money laundering in Nigeria and identifies the challenges ahead as well as the measures which will mitigate the wave of the crime in the country.

In order to achieve this, the paper is organized into six sections. Following this introduction, section II explains the conceptual issues relating to money laundering activities. Section III deals with country experiences and literature review on the economic effects of money laundering by examining each of the major economic sectors in turn. Section IV takes a specific look at money laundering in Nigerian economy, while section V presents the issues and challenges emerging from the review of the various efforts towards combating money laundering in the country. Section VI draws from the Nigerian and international experiences in proposing a package of measures to enhance the combating of these crimes in Nigeria before summarizing and concluding the paper.

II. Conceptual Issues in Money Laundering

To appreciate the need or otherwise for combating money laundering and other related crimes, it would be instructive to examine the meaning of the various concepts involved in this section.

II. 1 Money Laundering and Stages of Transactions

Conceptually, money laundering is the criminal's way of disguising the origin of his illicit money or financial assets so that detection and the risk of prosecution in its use could be avoided. Legally, it is defined as any attempt to engage in monetary transaction that involves criminally derived property (Bauer & Ullmann, 2000). Anti-money-laundering, therefore, is an effort designed to prevent or limit the ability of criminals to use their ill-gotten gains (McDowell and Novis, 2001). It is important to emphasise that effective anti-money laundering policies support a variety of other good-governance policies that assist in sustaining economic development, particularly through the strengthening of the financial sector.

Originally, the scope of money laundering activity was limited to proceeds from drug trafficking or proceeds from offences related to organized crime, but it has now been drastically expanded to cover other, if not all, types of proceeds of crimes. The dynamics of money laundering involves transforming the proceeds of crime into usable form and disguising their illegal origins. After the illicit proceeds are introduced to the financial system, they are hidden, laundered through a variety of transactions and financial vebicles and, finally, invested in financial and related assets. These operations often involve international transactions as a way of obscuring the source of the funds. Indeed, money laundering is intrinsically global. If one country or jurisdiction tightens its regulations on money laundering, the activity will quickly shift to a less regulated environment. Even a country with little crime and little money laundering needs to be proactive to avoid the immigration of the problem. Money laundering generally involves a series of multiple transactions used to disguise the source of the ill-gotten assets. These transactions typically fall into three stages that sometimes overlap:

i) **Placement:** This is the process of placing unlawful proceeds into financial institutions through deposits, wire transfers, or other means.
ii) **Layering:** At this stage, the launderer attempts to further obscure the trail of criminally generated funds by separating them from their origin through the use of complex financial transactions. For example, sophisticated criminals with large sums to launder, may set up big companies in countries known for strong

bank secrecy laws and transfer money among these companies until they are seemingly clean. These transactions must be disguised to blend in with other legitimate transactions that occur everyday. Loan backs and double invoicing are such other common techniques employed in the layering stage. With a loan-back, the criminal puts the funds in an offshore entity that he secretly controls and later, the funds are loaned back to him. This technique works because it is hard to determine who actually controls offshore accounts in some countries. In the case of double-invoicing, an offshore entity keeps two sets of books. To move clean funds into Germany for instance, a German entity overcharges for some goods or services. To move funds out (say, to avoid taxes), the German entity is undercharged. Other layering techniques involve the use of casinos because they readily take cash and once converted into chips, the funds appear to be winnings which are redeemable by a cheque drawn on the casino's bank (Bauer and Ullmann, 2000).

iii) **Integration:** This is the process of using an apparently legitimate transaction to disguise illicit proceeds. At this stage, the funds are moved into the mainstream of economic activities such as business investments, real estate or luxury goods purchases and others.

II.2 The Hawala System Informal Funds Transfer System

Informal funds transfer (IFT) systems are in use in many regions for transferring funds, both domestically and internationally. The hawala system is one of the IFT systems that exist under different names in various regions of the world. It is trust-based and is peculiar to people of Asian/Middle East origin. The hawala system refers to an informal channel for transferring funds from one location to another through service providers known as hawaladars. Since the September 11, 2001 terrorist attacks on the United States, public interest in the hawala system has increased, following its alleged role in financing illegal and terrorist activities along with its traditional role of transferring money between individuals and families, and often in different countries. A hawaladar from country A (HA) receives funds in one currency from a customer "CA" and, in turn, gives CA a code for authentication purposes. He then instructs his country B correspondent (HB) to deliver an equivalent amount in the local currency to a designated beneficiary (CB), who needs to disclose the code to receive the funds. HA can be remunerated by charging a fee or through an exchange rate spread. After the remittance, HA has a liability to HB, and the settlement of their positions is made by various means, either financial or goods and services. Their positions can also be transferred to other intermediaries, who can assume and consolidate the initial

positions settled at wholesale or multilateral levels.

The settlement of the liability position of HA vis-à-vis HB that was created by the initial transaction can be done through imports of goods or "reverse hawala". A reverse hawala transaction is often used for investment purposes or to cover travel, medical, or education expenses from a developing country. In a country subject to foreign exchange and capital controls, a customer (XB) interested in transferring funds abroad for, in this case, university tuition fees, provides local currency to HB and requests that the equivalent amount be made available to the customer's son (XA) in another country (A). Customers are not aware if the transaction they initiate is a hawala or a reverse hawala transaction. HB may use HA directly if funds are needed by XB in country A or indirectly by asking him to use another correspondent in another country, where funds are expected to be delivered. A reverse hawala transaction does not necessarily imply that the settlement transaction has to involve the same hawaladars. It could involve other hawaladars and be tied to a different transaction. Therefore, it can be simple or complex. Furthermore, the settlement can also take place through import transactions. For instance, HA would settle his debt by financing exports to country B, where HB could be the importer or an intermediary.

II.3 Directions of Money Laundering Flows

Five directions of money laundering flows could be evident in an economy and these include:

(i) **Domestic money laundering flows:** This is a process by which illegal domestic funds are laundered within the country's economy and reinvested or otherwise spent within the economy.

(ii) **Returning laundered funds:** Under this, laundered funds originating from a particular developing country formerly laundered partially or in full abroad are returned for integration in the originating country.

(iii) **Inbound funds:** This is a case for which the predicate crime occurred abroad are either initially laundered (placed) abroad or within the country, and ultimately are integrated into the economy.

(iv) **Outbound funds:** These typically constitute illicit capital flight from the economy and do not return for integration in the original economy.

(v) **Flow-through funds:** These enter the country as part of the laundering process and largely depart for integration elsewhere, thus playing little or no role in the economy itself (although the 'fees' for money laundering activity may remain).

II.4 Other Related Crimes

Other related economic and financial crimes range from conventional types such as embezzlement and breach of trust to new types such as collusive bidding, cartels, insider trading, market manipulation and internet crime which are increasingly getting more diversified, complicated and sophisticated.

III. Country Experience and Literature Review

III.1 Country Experiences

An extensive UN study of the effect of money laundering on Russia noted that in the Russian Federation, money laundering is always linked to the problem of capital flight and a subsequent lack of investments. It was estimated that the amount of illicit capital flight laundered from Russia in recent time exceeds $100 billion, implying an enormous drain on investment resources (UN Report 2001).

The U.S. Office of the Comptroller of Currency (OCC) recently levied a $20 million fine on Bank of China because its employees allegedly committed favoritism, irregularities, issued fraudulent letters of credit and facilitated loan frauds in the Bank's New York operations. Also, two branch managers and an assistant manager of the Bank of China at its Kaiping branch allegedly colluded with government officials and contractors in Hong Kong to defraud the Bank of $75 million. Following the disclosure of the incident, there was a run on the Bank's Kaiping branch. Consequently, the Bank of China's reputation suffered, and plans to list its Hong Kong subsidiary on public stock exchanges are now in question (Fang, 2002).

The French authorities in late 2001 launched a series of investigations into officials of France's leading banks in connection with fraud, tax evasion as well as money laundering. The subsequent report showed that thousands of French cheques, some of them stolen, were endorsed or signed over to new beneficiaries before being cashed at money-changers in Israel and the proceeds exceeding $70 million were returned to France through correspondent banking relationships (The Banker, 2000; The Jerusalem Post, 2001).

Following its bankruptcy in 1995, the Dusseldorf prosecutors investigated 10 former employees of a private bank, BVH on suspicion of fraud, disloyalty and money laundering, and discovered that the bank laundered funds in the form of bogus credits, and redirected them to a firm believed to bave belonged to Osama Bin Laden's Al-Qaeda network (Sonntag, am Welt, 2001).

III.2 Review of Literature on the Effect of Money Laundering

Although it is difficult to quantify the impacts of money laundering on economic development, yet it is clear that such activity has some damaging effects on the financial institutions which are *sine qua non* to economic growth. It also reduces productivity in a country's real sector by diverting resources and encouraging crime and corruption, which slow down economic growth. Furthermore, such activity can distort the economy's external sector through international trade and capital flows to the detriment of long-term economic development. In what follows, we shall attempt to review existing literature on these issues sector by sector.

In the view of Comley (2001), banks, equity markets and non-bank financial institutions (NBFIs), such as insurance companies have been identified as favoured means of perpetrating money laundering activities both internationally and within countries. The reason for this preference, according to him, lies in the efficiency of the financial institutions in providing funds for the actors of such crimes. He further noted that money laundering through financial institutions affects such institutions themselves in 3 broad ways: by increasing the probability that individual customers will be defrauded by corrupt individuals within the institution; by increasing the probability that the institution itself will become corrupt or even controlled by criminal interests; and by increasing the risk of financial failure faced by the institution as a result of the institution itself being defrauded. Such dangers, he stated, come under operational risk and can contribute significantly to reputational risks. A reputation for integrity, no doubt, is one of the most valued assets by investors. Money laundering activity constitutes clear operational risks to the financial soundness of an institution; adversely affects jurisdiction's reputation; undermines investors' trust in the economy; and above all weakens the financial system.

Furthermore, Strachan, Smith and Beedles (1983) have noted that financial institutions in the developing economies are often undergoing a transition from being state-owned to private-investor ownership and control, and as such investors are more reluctant to commit funds to obtain ownership in enterprises cited for corruption, particularly money laundering activities. Also, from a developing country's policymaking standpoint, he observed that a country with lax anti-money-laundering enforcement measures can be subject to formal legal sanctions by important trade and investment partners.

Molina (1995) in his study has noted that apart from its impact on countries' financial sectors, money laundering also has more direct effects on economic growth in the real sector through the following ways: by diverting resources to less-productive activity

or investments that generate little additional productivity for the broader economy such as jewelry, luxury automobiles and real estate, money laundering activity tends to depress growth in an economy. For developing countries, the diversion of such scarce resources to less-productive domestic assets or luxury imports is a major obstacle to economic growth.

He further noted that criminal organizations can transform productive enterprises into sterile investments by operating them for the purposes of laundering illicit proceeds rather than as profit-maximising enterprises responsive to consumer demand and worthy of legitimate investment capital. He stated that the content of trade, particularly imports can also be warped by money laundering activity. For example, a corrupt official may decide to launder his illicit funds outside the country and return the proceeds to the country for his own consumption and enjoyment. Money laundering also facilitates corruption and crime within developing economies, which in turn depresses growth.

Unabated money laundering can also impair a developing country's economy through trade and international capital flows. Loungani, and Mauro, (2002) commenting on capital flight from Russia noted that a money laundering technique that does not directly involve the financial system or expenditures in the real domestic economy is the use of inaccurate pricing (miss-invoicing or over invoicing) of imports or exports to hide the transfer of funds during the layering process within what appears to be a value-for-value transaction. When such transactions are extensive, he noted, the impact on a country's entire external sector can be substantial.

As recently noted by the IMF, money laundering activity can through reputational effects affect the willingness of economic agents, particularly those outside the country to conduct businesses like inward investment, banking correspondent relationships, among others, in a particular country with its adverse consequences. The effects of money laundering on foreign investment are much because of its blockage of special benefits such as technology, labour skills and know-how, and immediate access to international distribution channels that such foreign resources bring to developing economies.

According to the Brooking Event Transcript (1999), money laundering has been identified as a key element in illicit capital flight from developing countries. He observed that the massive illicit capital flight from Nigeria since the mid-1990s made full use of money-laundering centers in the developed world, and were largely not being repatriated, contrary to the notion that money laundering is a problem involving illicit developed country funds being laundered in the developing world.

Abbott (2000) asserts that for most developing countries, the creation of an off-shore financial center (OFC) is seen as a panacea for their economic disadvantages. Specifically, many OFCs have been created as part of developing countries' efforts to develop their domestic economies through the provision of international financial services.

In contrast, Palan and Abbott (1996) have asserted that the Bahamas was the third largest offshore banking center in the world, but by the end of the 1980s, had fallen to 11th place as a result of widespread publicity concerning drug trafficking and corruption of its institutions. In an extreme case, Panama's growth as an OFC was reversed as the volume of money laundering expanded to such levels that the entire financial system was viewed as corrupt, and funds were massively moved from the country's financial system even before the U.S government began applying sanctions against it.

IV. Money Laundering: The Nigerian Experience

Historically, the insurgence of money laundering activity in Nigeria dates back to the declining fortunes of the oil boom, following the collapse of prices in the international oil market in the 1980s and the ensuing austerity measures associated with the country's Structural Adjustment Programme. This has since then encouraged unprecedented greed and avarice, resulting in grave crimes like corruption, fraud, armed robbery, ritual killing, assassination, drugs peddling, prostitution, advance fee fraud (a.k.a "419"), money laundering, currency counterfeiting, oil bunkering, hank fraud, illegal contract deal, e-mail scam and other such related crimes, among Nigerians. Regrettably, these nefarious acts resulted in decreased productivity and negatively impacted on the image of Nigerians as crooks and dupes in the international circle. While efforts have been made by international agencies to combat money laundering, the crime seems to be gradually eating deep into the economic fabrics of Nigeria.

In 2000, Nigeria was adjudged by the Financial Action Task Force (FATF), a Paris-based anti-money laundering body, as one of the non-cooperative countries or territories (NCCTs) in the fight against money laundering. Prior to FATF's assessment, Transparency International had categorized Nigeria as one of the most corrupt in the world. Also, the UK's financial supervisory authorities estimated that illicit transactions in UK accounts that originated from Nigeria amounted to about $1.3 billion between 1996 and 2000. There are numerous cases of money laundering in the country. A few of them are proven cases. A large number of them are still being

investigated, while others are being prosecuted. A few of the proven cases include a deceased legislator in the lower house of the National Assembly and the celebrated case of a Nigerian widow involving a Brazilian nationale, among others.

In realization of the adverse consequences of such brazen crimes on the economy, particularly now that the country is striving for economic rebirth, the Federal Government in March 2003 inaugurated the Economic and Financial Crimes Commission (EFCC) and charged it with the responsibility of investigating economic and financial crimes in the country and bringing the perpetrators to book. Interestingly, the EFCC has all what it takes to tackle head-on the hydra-headed monster of economic and financial crimes in the country as the Commission was established by an enabling Act of the National Assembly in December 2002. Of more paramount importance is the recognition of EFCC by the FTAF, a reputable international body that is committed to combating economic and financial crimes around the world. Under Section 7 (2) of the EFCC (Establishment) Act, 2004, the Commission is the coordinating agency for the enforcement of the Money Laundering (Prohibition) Act, 2004. The EFCC has a 21-member board drawn from the law enforcement agencies (LEAs), regulators and the private sector, including the Nigerian Police, the Department of State Security Services (SSS), the Nigeria Customs Service, National Drug Law Enforcement Agency (NDLEA), Central Bank of Nigeria (CBN), Nigeria Deposit Insurance Corporation (NDIC), Corporate Affairs Commission (CAC), the Nigeria Postal Service (NPS), National Insurance Commission (NAICOM), the Securities and Exchange Commission (SEC), the National Intelligence Agency (NIA), Representatives from the Federal Ministries of Justice, Foreign Affairs and Finance, the Nigerian Communications Commission (NCC), the Nigeria Immigration Service (NIS) and 4 members representing the private sector. The EFCC is also the parent body of the Nigeria Financial Intelligence Unit (NFIU), which is the central body for collecting and analyzing all financial data, including suspicious transactions reports from all financial institutions and designated non-financial institutions for the purpose of developing intelligence packages for law enforcement agencies and regulatory/supervisory bodies.

IV. 1 Methodological Issues And Analysis on Money Laundering

Empirical data on money laundering is scanty and this study provides a novel step towards a quantitative insight into the effects of money laundering on the economy. The discussion below highlights two key univariate time series decomposition techniques for the purpose of bringing out the severity of the problem. Other ratios were also considered in order to identify what proportion of the GDP is a cost associated with money laundering activities.

In the decomposition of the Univariate time series data, two methodologies used in the framework could be identified, namely, the Beveridge-Nelson decomposition and the Hodrick-Prescott filter. Suffice it to say that while the multivariate framework is at the vortex of discussions of modern macroeconometrics, the univariate framework will now be succinctly discussed and fitted into the current study as the multivariate framework techniques are beyond the scope of this study. Such an application to money laundering is novel and would provide intuitive insight into the intensity of money laundering in Nigeria based on banks' foreign assets portfolio.

Beverigde and Nelson (1981) provide an elegant way of decomposing a non-stationary time series data into a permanent and a temporary (cyclical) components by applying autoregressive integrated moving average (ARIMA) methods. For any non-stationary time series x_t, integrated of the first order, the Wold decomposition theorem could be applied to its first difference, to deliver the following representation:

$$\Delta x_t = \mu + C\,(L)\,\varepsilon_t,$$
$$\varepsilon_t \sim n.i.d.\ (0, \delta^2_{\varepsilon}),$$

where C(L) is a polynomial of order q in the lag operator. The final equation can take the form

$$\begin{aligned} x_t &= C^*\,(L)\,\varepsilon_t + \mu t + C\,(1)\,z_t, \\ &= C_t + TR_t, \end{aligned}$$

where z_t is a process for which $\Delta z_t = \varepsilon_t$. C_t is the cyclical component and TR_t is the trend component made up of a deterministic and a stochastic trend. The trend component could be represented as:

$$TRt = TRt\text{-}1 + \mu + C\,(1)\,\varepsilon_t.$$

The Hodrick-Prescott (HP) filter was proposed by Hodrick and Prescott (1997) to analyze postwar US business cycles in a working paper circulated in the early 1980s and published in 1997. The filter computes the permanent component, TR_t of a series x_t by minimizing the variance of x_t around TR_t, subject to a penalty that constrains the second difference of TR_t. The expression minimized to derive the filter is given by

$$\sum_{t=1}^{T}(x_t - TR_t)^2 + \lambda\sum_{t=2}^{T-1}\left[(TR_{t+1} - TR_t)^2 - (TR_t - TR_{t-1})^2\right]$$

The penalty parameter λ controls the smoothness of the series, by controlling the ratio of the variance of the cyclical component and the variance of the series. The larger the λ, the smoother the TR_t approaches a linear trend. In practical terms λ is set to 100 for annual data, 1600 for quarterly data and 14400 for monthly data.

Evidence suggests that the Beveridge-Nelson trend is more volatile than the Hodrick-Prescott trend (Favero, 2001). It is plausible for the volatility of the Hodrick-Prescott trend to increase by reducing the parameter λ. However, the Hodrick-Prescott filter reaches at most the volatility of the actual time-series, which is smaller than the volatility of the Beveridge-Nelson trend (Favero, 2001). Though Harvey and Jaeger (1993) showed that the use of the HP filter could lead to the identification of spurious cyclical behaviour, a key advantage of the filter is that of removing the same trend from all time-series.

IV. Relevance of the HP Filter in the Study of Money Laundering

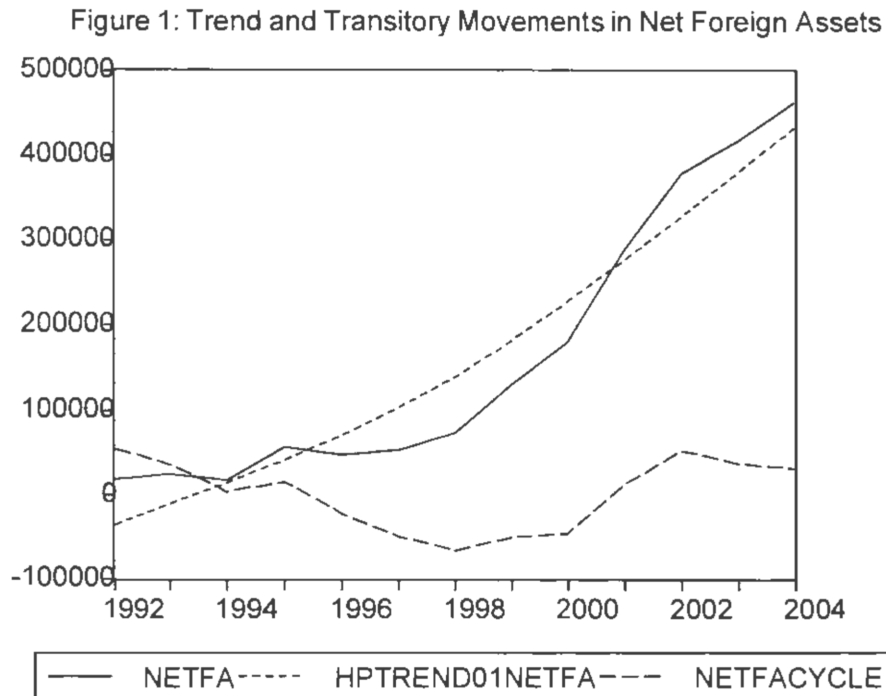
Money launderers subvert legitimate financial mechanisms and banking relationships by using them as protective covering for the movement of criminal proceeds and the financing of crime and terrorism. By so doing, money laundering undermines the integrity of global financial and trading systems upon which prosperity and growth depend. Anecdotal evidence show that transactions involving such offshore jurisdictions make it difficult for law enforcement officials and regulators to follow the trail of money earned by criminals, organized international criminal enterprises, and global terrorist organizations. Correspondent banking facilities are one of the banking mechanisms susceptible in some circumstances to manipulation by foreign banks to permit the laundering of funds by hiding the identity of real parties in some financial transactions. Thus, private banking services can be susceptible to manipulation by money launderers, for example corrupt foreign government officials. This is particularly so if those services include the creation of offshore accounts and facilities for large personal funds transfers to channel funds into accounts around the globe. In view of this, foreign assets holdings of banks become the hub for concealment of money laundering transactions. Since it has been a difficult exercise even for regulators to break-in on suspicion of banks activities in perpetuating money laundering, the Hodrick-Prescott (HP) filter provides a prima facie evidence of the severity of the problem. This scenario is typical of the United States where anti-money laundering efforts are impeded by outmoded and inadequate statutory provisions that make investigations, prosecutions, and forfeitures more difficult, particularly in cases in which money laundering involves foreign persons, foreign banks, or foreign countries. The HP filter enables the identification of the irregular components of banks foreign assets holding as it moves away from its trend path. This is why, for instance, in the European Union countries, credit institutions are expected to ensure that their associated companies, in particular financial services institutions and financial institutions comply with their respective duties under the Act. Locally

resident branches of foreign credit institutions are also subject to the Money Laundering Act. The next section experiments with the filter and discusses it in the context of the role which money laundering activities play on the Nigerian economy.

IV.3 Money Laundering Activities in Nigeria Between 1992 and 2004

Evidence from the HP filter on the net foreign assets (NFA) of the deposit money banks (DMBs) in Nigeria (see figure 1), indicated that between 1992 and 1995 when money laundering was evidently criminalized in the country, the level was above its potential level.

Source: CBN Statistical Bulletin, 2003



Key:
NETFA: net foreign assets
HPTREND01NETFA: Trend or potential Component
NETFACYCLE: Cyclical or fluctuations around trend

This was reminiscent of the high volume of investible resources held-up by the DMBs in their correspondent banks overseas. The Anti-Money Laundering Act No.3 of 1995, which institutionalized information disclosure by the banks, however, led to a significant decline in the level of banks' NFA between 1995 and 2001. This period clearly indicated that without the activities of money launderers, the DMBs were largely insulated and un-integrated into the global financial architecture as it was evident that the banks, within this period could not attain the potential level of their NFA. Banks' level of NFA again surged between 2001 and 2004, reflecting the institutional weaknesses in the enforcement of the various anti-money laundering Acts (fig.1). The banks became havens for transferring ill-gotten funds abroad through the use of diplomatic covers to exploit laws with a view to escaping prosecution.

Anecdotal evidence on Nigeria collaborate the above trend and puts the number of arrest on money laundering cases since 1995 at 2469, while the number of prosecutions and convictions were respectively, 154 and 12. The estimated value of laundered money from Nigeria is put at an annual average of ₦10 billion, representing 0.012 per cent of the country's GDP (2004 current basic prices) and 2.4 per cent in real term. These figures are scaring compared with global losses associated with the crime. For instance, money laundering has been estimated by the International Monetary Fund to amount to between 2 and 5 percent of global gross domestic product, which is at least $600,000,000,000 annually.

For the avoidance of doubt (see Table 1), bi-annual findings of the Nigerian Financial Intelligence Unit (NFIU) of the Economic and Financial Crimes Commission (EFCC) (Ribadu, 2005) indicate that 10 out of the 92 reporting institutions including banks accounted for 100 and 97.7 per cent of all suspicious transactions reports (STRs) by the first and second quarter of 2005, respectively. By the first six months of 2005, 25 banks accounted for 84.4 per cent of currency transactions reports (CTR) renditions received by the NFIU. In terms of absolute numbers, the NFIU received 1,299 STRs, 1,324,592 CTRs and 64,573 financial transactions reports (FTRs) in the first 6 months of the year.

Table 1: Rendition to NFIU for the First Half of 2005

Period	STR	CTR	FTR
First Quarter of Year 2005	346	481,920	19,973
Second Quarter of Year 2005	953	842,672	44,600
First Half of Year 2005	1,299	1,324,592	64,573

IV.4 Review of Efforts towards Combating Money Laundering and Other Related Crimes in Nigeria

Nigeria has long realized the adverse effects of money laundering and other related crimes and the fact that it was in her interest to actively participate in the fight against these crimes. In this regard, the country has adopted various strategies aimed at combating them. For instance, Nigeria passed an Anti-Money Laundering Act in December 2001, which expanded the scope of the earlier one of 1995 from drugs to any crimes or illegal act. These, however, excluded certain anti-money laundering obligations to non-bank financial institutions, and the need to extend customer identification requirements to include occasional transactions of $500 or more. Nigeria followed up by enacting the Economic and Financial Crimes Commission (EFCC) Act in December 2002 with far reaching functions and powers which cut across crimes involving advance fee fraud, money laundering, counterfeiting, illegal charge transfers, futures market fraud, fraudulent encashment of negotiable instruments, computer credit card fraud, and contract scam, among others. The country took another step by enacting the Money Laundering (Prohibition) Act 2004, which consolidated the previous anti-money laundering legislations and provided a broader interpretation of financial institutions and scope of supervision of regulatory authorities on money laundering activities.

The strategies already taken by the country in the fight against money laundering and other related crimes are as summarized below:

- The establishment of the National Drug Law Enforcement Agency (NDLEA) in 1990 by Decree No. 48 to check drug-trafficking and its associated money laundering activities.
- The establishment of a special fraud unit within the Nigeria Police charged with the responsibility of investigating and prosecuting cases bordering on criminal deception or advance fee fraud.
- The setting up of the Money Laundering Surveillance Unit in the Central Bank of Nigeria in 1994. The Unit is charged with the responsibility of ensuring that the banks and other financial institutions comply with the provisions of the Money Laundering Guidance Notes, Money Laundering Act and observe the "Know Your Customers" directives issued by the CBN.
- The enactment of the Failed Banks (Recovery of Debts) and Financial Malpractices in Banks Act No 18 of 1994 aimed at trapping the officials and customers of banks who had looted the banks' treasury.
- The promulgation of the Advance Fee Fraud and other Fraud Related Offences Act No 13 in 1995.
- The appointment of a Special Adviser to the President on Drugs and Financial Crimes and the establishment of the high-powered Inter-Ministerial Committee on Crimes.
- The establishment of the Financial Services Regulation Coordinating Committee (FSRCC) in 1998, comprising the Central Bank of Nigeria, Securities and Exchange Commission, National Insurance Commission, Corporate Affairs Commission and Federal Ministry of Finance. The Committee co-ordinates the supervision of the financial institutions in the country and shares information on areas of corruption and fraud practices relating to their customers as well as employees.
- The establishment of the Independent Corrupt Practices Commission (ICPC) to implement the anti-corruption law of the Federal Republic of Nigeria.
- Money Laundering (Prohibition) Act 2004.

The Money Laundering (Prohibition) Act 2004 and for matters connected therewith seeks to:

- Provide for the repeal of the Money Laundering Act, 2003;
- Make comprehensive provisions to prohibit the laundering of the proceeds of crime; and
- Provide appropriate penalties and expand the interpretation of financial institutions and scope of supervision of regulatory authorities on money laundering activities, among other things.

The major provisions of the 2004 Act included:

- Limitation to make or accept cash payment;
- Duty to report international transfer of funds and securities;
- Identification of customers; special surveillance on certain transactions; preservation of records;
- Arousing awareness among employees of financial institutions; mandatory disclosure by financial institution; liability of directors, etc. of financial institutions;
- Surveillance of bank accounts, etc; and other offences.

The details of these major provisions of the 2004 Act can be found in the original document.

IV.5 The Effects of Money Laundering on the Nigerian Economy

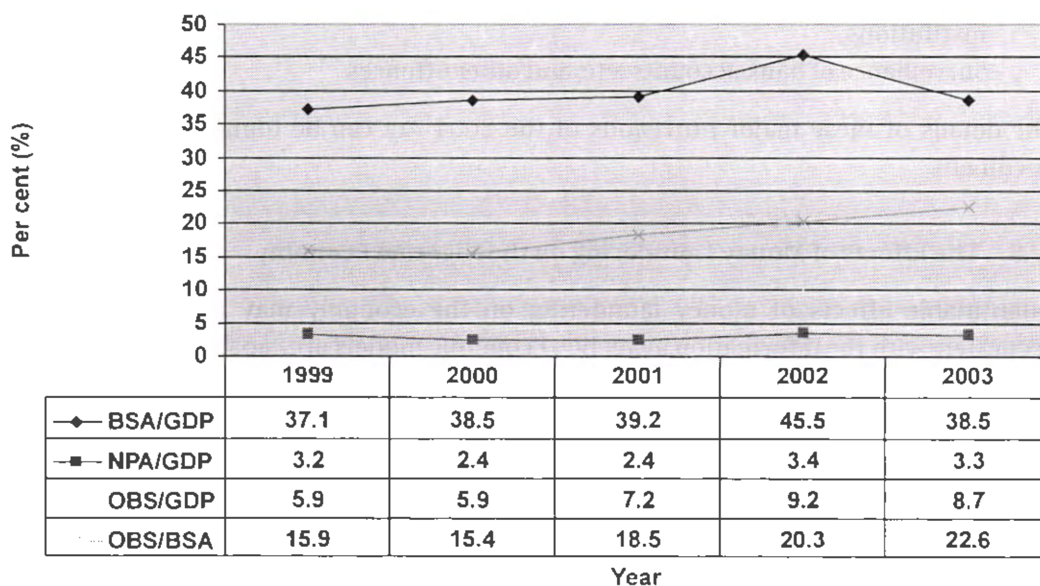
Quantifiable effects of money laundering on the economy may not be assessed accurately with the information available. Economic models are capable of tracing the multiplier effects of money taken from one sector of the economy and spent in another sector, but there is little systematic data on how laundered money is spent. When illicitly gained money is spent on lavish real estate, there is probably a net loss to the economy, but where it is turned into legitimate businesses, the net effects can be quite positive to the economy. The perceived costs to the Nigerian economy, however, could be discussed in the context of international best practices vis-à-vis the characteristics and vulnerabilities of the economy. In view of this, the centre-piece of the discussion is the financial, real and external sectors of the economy.

In the first place, money laundering has the potential of accelerating banking system distress: financial institutions are conduit for matching investors' and savers' needs through the intermediation process.

Money laundering in Nigeria has, however, increased reputational risks of banks as most of them are after hot money, without minding the source, thereby abandoning their traditional role of intermediation. This perhaps is one of the reasons why banks keep large proportions of their transactions off-balance sheet. Insight into this behaviour can be seen from figure 2. The period 1999-2003 for which the net foreign assets increased above its potential level (fig 1) correlates with the period that both the banking system's total assets and off-balance sheet transactions averaged 39.8 and 7.4 percent of GDP, respectively, (fig 2). As a catalyst for systemic crisis, the period also reflected that the significant proportion of its assets were in non-performing assets

(NPA) which averaged 2.9 per cent of GDP. Thus, there are renewed possibilities that individual customers will be defrauded by individuals and their crony institutions. The consequence is to undermine investor confidence in the financial system, especially in the context of weak legal system that could hardly compel enforcement of anti money laundering laws.

Figure 2: Some Selected Ratios On Bank Behaviour



	1999	2000	2001	2002	2003
BSA/GDP	37.1	38.5	39.2	45.5	38.5
NPA/GDP	3.2	2.4	2.4	3.4	3.3
OBS/GDP	5.9	5.9	7.2	9.2	8.7
OBS/BSA	15.9	15.4	18.5	20.3	22.6

N.B
BSA/GDP represents the ratio of total banking system assets to GDP
NPA/GDP is the ratio of non-performing assets of banks to GDP
OBS/BSA is the ratio of off-balance sheet items to banking system assets
OBS/GDP represents the ratio of off-balance sheet item to GDP

Capital flight, in addition to expenditure switching into less productive areas due to money laundering, has starved the real sector of investment funds with the consequence of denying growth in the emerging small business enterprises in the economy. Very recently, public opinions have indicated how highly placed bureaucrats fingered to be money launderers invest in real estate involving several billions of naira in the country. Indeed, laundered money has been used to fund illegal businesses like drug counterfeiting and other related crimes in the country. All these inhibit growth and undermine human capital development. This is fundamentally so because money

laundering has encouraged corruption and crime to the detriment of boosting a more vibrant manufacturing sector of the economy.

More fundamentally, money laundering poses substantial volatility on Nigeria's exchange rate and constrains the growth of foreign direct investment. It has been observed that the naira exchange rate differential reflects to a large extent a premium that purchasers of foreign exchange are willing to pay to falsify import documents so that they could evade custom duties, or to make transfers that were otherwise restricted or illicit. This means that the demand for foreign exchange could be inflated by money-laundering activities using trade channels, driving up the price of foreign exchange. By driving up the Nigerian exchange rate, the mere technique of using trade as a money laundering technique had reduced the competitiveness of Nigerian exports on world markets, thus slowing the country's economic growth (see IMF Staff Report on Nigeria, 2001). Again, in Nigeria, money launderers are being prosecuted today by the Economic and Financial Crime Commission (EFCC) for using illicit funds outside the country to import luxury vehicles in a bid to return the proceeds to the country for their own consumption. The process of integrating rather than repatriating the funds abroad by importing foreign goods switches growth-enhancing domestic demand to imports thereby precipitating macroeconomic volatility in the country.

In addition, the reputational effects of money laundering affect the willingness of economic agents, particularly those outside the country to conduct businesses like inward investment, banking correspondent relationships, among others, with its adverse consequences on the economy. The effects of money laundering on foreign investment in Nigeria are substantial because of its blockage of special benefits such as technology, labour skills and know-how, and immediate access to international distribution channels that such foreign resources could bring to the country. For instance, the massive illicit capital flight from the economy since the mid-1990s made full use of money-laundering centers in the developed world, and were largely not being repatriated, contrary to the notion that money laundering is a problem involving illicit developed country funds being laundered in the developing world.

Again, Nigeria being on the list of NCCTs of the Financial Action Task Force means that the country is considered a high-risk country to make financial transactions in, and the implication is that international financial institutions often impose premium charges on transactions involving Nigerian financial institutions. Also being on the list often makes it very difficult for Nigerians living overseas to open accounts, especially in branches of multinational financial institutions as FATF had warned that special

attention should be given to business relations and transactions with persons, including companies and financial institutions from the NCCTs.

There are other significant social costs and risks associated with money laundering in the country. Money laundering allows drug traffickers, smugglers and other criminals to expand their operations. This is capable of driving up the cost of governance due to the need for increased law enforcement and health care expenditures (for example, for treatment of drug addicts) to combat the serious consequences that it brought into society.

Again, money laundering transfers economic power from the market, government and citizens to criminals. Furthermore, the sheer magnitude of the economic power that accrues to criminals from money laundering has a corrupting effect on all elements of the society. In extreme cases, it can lead to the virtual take-over of legitimate government. Overall, the possible social and political costs of money laundering on the Nigerian economy, if left unchecked, are capable of weakening the social fabrics, collective ethical standards, and, ultimately the democratic institutions of the society.

V. Emerging Issues and Challenges

Despite the various approaches adopted by the country in the fight against money laundering and other related crimes, and the successes achieved so far, the incidence of financial crimes continues to persist, while the rate of prosecution and conviction is rather slow. This is because of the complex nature of the phenomenon and the challenges Nigeria is facing in its enforcement efforts.

V.1 The Regulatory Challenge

The anonymity enjoyed by the operators in the unregulated business activities in Nigeria facilitates the perpetration of these crimes. There are a number of handicaps facing the Nigeria Police such as operational logistics, funding, training, motivation, manpower and combat equipment. In addition, the phenomenal advances in technology, which have exposed our economy to various forms of economic and financial crimes; and the increasingly sophisticated equipment and methods used by the perpetrators in their nefarious activities, give them greater advantage ahead of the law enforcement agents in the country. Specifically, limited technology and infrastructure at the disposal of the regulatory and law enforcement authorities in the country make detection of crimes and prosecution of criminals extremely difficult. There is, therefore, need to provide the law enforcement authorities and other

regulatory agencies with up-to-date equipment to enable them to be alive to their responsibilities.

V.2 Legal Reforms

The constraint imposed by the requirements of the Nigerian law poses a great challenge for the fight against money laundering and other related crimes in the country. Nigeria operates the common law criminal jurisprudence of presumption of innocence, and the requirement of the rules of evidence pushes the burden of establishing the guilt of an accused person to the prosecution (Sections 95 and 97 of the Evidence Act of Nigeria). This makes the testimony of victims of crimes, particularly in cases of advance fee scams vital in criminal proceedings. This differs from the French jurisdiction which declares an accused person guilty until proven otherwise.

Allied to this, is the slow pace of the judicial process due largely to under-staffing and obsolete procedures. There is also the associated difficulty of tendering electronic documents as evidence under the Nigerian Law of Evidence in the prosecution of money laundering cases. For instance, it is arguable whether a computer printout qualifies as documentary evidence and if so, under what class of documentary evidence it is to be categorized. The argument is held on the premise that such a printout cannot be described as the original document as the data on it was retrieved from some other storage medium, e.g., hard or floppy disk. Likewise, since the original is in some "object" or machine code form, a printout, which is produced in a different form cannot be said to be a copy of the original.

This unsettled state of the law, regarding admissibility of computer-generated evidence, requires urgent legislative intervention before international criminals turn Nigeria to a haven for digital or cyber cash laundering. Furthermore, limitations of domestic forfeiture laws can lead to complex and time consuming legal issues with respect to jurisdiction and the venue for the forfeiture case. This is particularly true in cases in which the Nigerian law enforcement agency does not know initially the final destination or beneficiary of the funds sent through a correspondent account and only discovers this fact at a later point in time.

V.3 The Payments System and e-Banking Challenge

The poor banking habit among Nigerians and the cash and carry orientation of the economy remains the greatest asset to money launderers and, thus, a predicament to an effective ant-money laundering policy in the country. Though the Money Laundering Act prohibits cash transactions above ₦500,000 and ₦2,000,000 for

individuals and companies, respectively, and requires the reporting of banking transactions above these limits to the EFCC/NDLEA, the practicability of such regulations is doubtful, especially in a cash and carry economy like Nigeria. Such regulations, no doubt, can be effective in countries with advanced financial systems where large cash transactions are unnecessary and, thus, naturally raise suspicion. The same cannot be said of Nigeria where large cash transactions, though unsafe, are not uncommon due to lack of confidence in the financial system. In addition, due to our low level of technological advancement, internet usage has been a source of financial fraud in the country. As long as people are not exposed in the use of the modern electronic means of payment, the problem will continue to linger.

V.4 The Challenge of Globalization and Good Corporate Governance

The use of correspondent banks poses a great challenge for anti-money laundering law enforcement officials in the country as they often encounter difficulty while trying to determine the actual location of the laundered funds as well as the jurisdiction to focus for future efforts. Even where law enforcement agents request the assistance of the correct foreign jurisdiction, the ability to forfeit these funds depends upon the strength of the forfeiture laws in that jurisdiction, which if available, may be incompatible with the home country law. It may also depend upon the cooperation of the foreign government as currently being experienced in the country. The challenge for the country, therefore, lies in reforms that will create partnerships or memoranda of understanding to be able to track and deal with this issue. As long as there are existences of legal and enforcement gaps in the country, the fight against international dimension of money laundering may remain elusive.

V.5 Cross-border Jurisdictional Issues

As money laundering crimes frequently transcend border, the issue of the appropriate jurisdiction in which to commence legal actions is a crucial one for a victim seeking to initiate action against the offender. The most common method to find jurisdiction is by service of process. This is easy if the defendant is within jurisdiction. In the cases of international criminal proceedings, there is a strong possibility that the court applied to, will be reluctant to exercise its jurisdiction on the ground that there is a more appropriate forum (or that it is a *forum non conveniens*) for the action. Again, there is a strong possibility of a court's reluctance to grant extradition of the offender. Although there are principles of conflict of laws to decide in what circumstances jurisdiction should be exercised, the conflict of law principles also differs from country to country. This could result in the victim going from court to court in search of a suitable jurisdiction, the possibility of which is likely to be a strong deterrent to

taking any legal action. The near mirage of not getting justice in the face of jurisdictional problems makes the fight against money laundering difficult. Again, only through international cooperation and synchronization of international laws that relative success could be achieved in the country.

V.6 High-Tech Transnational Issues

As the use of Internet and other new technologies increase, more money launderers are provided with opportunities to commit such crimes remotely, via telephone lines and data networks. Presently, malicious programming code and harmful communication pass through several carriers located in different countries. As banking and finance infrastructures are increasingly becoming networked, there is the possibility of them being vulnerable to cyber-attack from distant locations. This poses a great challenge in the efforts to combat money laundering activities. There is, therefore, the need to ensure that people are protected from those who use new technologies for financial and other related crimes anywhere in the world.

VI. Policy Recommendations, Summary and Concluding Remarks

VI.1 Policy Recommendations

The need for strict anti-money laundering policies in the country cannot be overemphasized. To achieve this would require:

Enhanced Resources for Financial Institutions Supervision

Sufficient resources should be devoted to the surveillance of the financial institutions, the enforcement of anti-money laundering standards, and cooperation with overseas authorities through innovative technology; reinforcement of good corporate governance in the financial institutions; reforms of the legal, financial and law enforcement structures in the economy; public enlightenment and on-going training of staff of financial institutions on the money laundering activities; and the need for global cooperation in implementing money laundering laws and jurisdictional issues involved. Financial institutions constitute key element in the perpetration of financial crimes and in the trail and detection of proceeds of criminal activities. This is because of their unique role in the payments system and the collection and transfer of financial assets and instruments. Bank supervisors should, therefore, play a leading role in this crusade, due to the increasing abuse of the financial system in the perpetration of financial crimes and the danger posed to the integrity of the system. The need for

increased surveillance of the financial system can, therefore, not be over-emphasized. The establishment of the Financial Services Regulation Coordinating Committee is, in this regard, a welcome development as it will facilitate the much needed co-ordination among regulatory bodies and, thus, help to eliminate regulatory arbitrage.

Training and Re-Training of Bank Staff on Money Laundering Techniques

Banks should conduct ongoing training programmes for their staff to review money laundering techniques, anti-money laundering procedures, charges in applicable laws and regulations and the kind of transactions that may warrant investigations. This regular training should also include how to identify and follow up on unusual or suspicious activities. The banks should train, not only all personnel who have account relationships but also appropriate back office personnel. In addition, all new employees should be provided with guidelines concerning anti-money laundering procedures and should be made to sign an attestation that he or she has read them. Evaluations of personnel should include how well each employee adheres to the banks' anti-money-laundering policy. Transactions or transfers in excess of a stipulated amount should be reported to the regulatory bodies promptly.

Good Corporate Governance Issue

Beyond protecting financial institutions from the negative effects of money laundering such as erosion of confidence, the adoption of anti-money-laundering policies by government financial supervisors and regulators, as well as by banks and NBFIs, can reinforce the other good-governance practices that are important in confidence building as well as the development of the financial institutions.

Improved Legislation

The necessary legal, financial and law enforcement structures must be in place in order to combat money laundering and other related crimes. The forty recommendations plus nine other special recommendations of the FATF, which is the accepted international standard in this regard, outline the steps that countries must take to protect themselves from money laundering abuse. For instance, FATF recommends that each country must ensure that its own law enforcement agencies, regulators, and judicial system are communicating, sharing vital information, and working together. In addition, the full range of regulatory measures such as comprehensive bank supervision and a system of suspicious activity reporting are necessary to deter and dictate money laundering.

International Cooperation and Exchange of Information

The authorities responsible for anti-money laundering, tax and financial regulations are expected to cooperate closely to combat cross-border financial crime, tax evasion and regulatory abuse, respectively. These authorities should permit effective routine supervision of the cross-border activities of financial institutions. The authorities should actively participate in international and regional seminars and conferences to increase knowledge and cooperation against economic and financial crimes. Indeed, it is important that the nations of the world work together to exchange information and to provide corporation in investigation and access for future cases. In the US for instance, it is the policy and practice, pursuant to statutory authority, to share the proceeds of success forfeiture actions with countries that made possible or substantially facilitated the forfeiture of access under US law (Lester, 2001). We believe that assets sharing among countries enhance international forfeiture actions by creating incentives for countries to work together, regardless of where the assets are located or which jurisdiction will ultimately enforce the forfeiture order. Only by working together at the international levels will we be able to stem the flow of criminal proceeds and cripple criminal organizations.

Cross-border Jurisdictional Issues

The issue of the appropriate jurisdiction in which to commence action against the perpetrator of an international money launderer should not arise so long as the assets are present within the jurisdiction. Courts should also be sensitive in deciding an application for extradition or of *forum non conveniens.*

Now that the Money Laundering (Prohibition) Act 2004 is in place, the greatest challenge facing those involved in the nefarious act of money laundering in the country is to embrace honesty, probity, accountability and transparency in all their dealings. In addition to this is the overriding necessity to exude the spirit of hard-work and industry, which generates productivity and progress in human society. Also, to fortify the Economic and Financial Crime Commission (EFCC) and make it not go the way of other agencies that initially started well but later lost steam, the Federal Government should show strong political leadership in the funding of the commission. Accordingly, the EFCC should be provided with office headquarters and zonal offices, along with reliable working materials. The staff of the EFCC should be adequately motivated through economic means like attractive salaries and allowances given the sensitive nature of the job they perform which requires high level of integrity and confidentiality. While the Federal Government is being urged to put in place a

macro-economic framework that repels poverty and economic disillusionment, which are the major factors leading some people into such crimes, it is expected that Nigerians would give the Commission the much-needed cooperation and support to enable it succeed.

VI.2 Summary and Concluding Remarks

This paper has reviewed in general the activities of money launderers and argued strongly that money laundering activities do not only harm individuals, but also sometimes cause great loss to public property, and could result in damaging of investors' confidence in doing business in a particular country, leading them to invest elsewhere. In the paper, it was established that money laundering constitutes a problem to Nigeria's economic development efforts. To this end, a review of efforts towards combating money laundering and other crimes in Nigeria was carried out in the paper. Some issues and challenges emerging from the country's efforts towards combating money laundering were also examined. The paper, therefore, concluded by calling for a technologically driven regulatory framework, reforms of the existing law of evidence to tackle electronic dimension of money laundering and domestic forfeiture laws, enhanced resources for financial institutions supervision, training and re-training of bank staff on money laundering techniques and finally, a need for global cooperation in implementing money laundering laws and jurisdictional issues.

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