

# U4 Expert Answer



## Evidence of illegal cross-border flows of funds, goods and services in South Asia and their impact on corruption

### Query

***What evidence exists on the issue of illegal cross-border flows of funds, goods and services in South Asia (Pakistan, India, Nepal and Bangladesh) and their impact on corruption? Please provide specific case studies of these processes in action.***

### Purpose

We are considering funding a programme to address bad governance in South Asia. Anecdotal evidence suggests illegal cross-border activities that feed corruption are a major problem. We are asking this question in an attempt to understand how empirical research supports this.

Illicit cross-border flows, also referred to as illegal flows, involve a network of actors and different countries. They also tend to overlap, meaning that the same groups that are smuggling drugs also tend to be the ones controlling arms and human trafficking. These networks also are often transnational, linking up local actors with a much broader web of players in other regions.

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Global evidence from other regions, such as Africa and the Caucasus, suggests that these networks take advantage of existing weak governance and corruption in a country to establish their operations. At the same time, by bringing the country into their network, corruption is worsened as it becomes the medium for ensuring the movement of illicit flows.

### Summary

The illegal flow of funds, goods and services, and people within and across borders plagues numerous countries and regions in the world. In Asia, the borders that Bangladesh, India, Nepal and Pakistan share with each other and neighbours have exposed them to these movements and the challenges that they bring. Among these challenges is corruption, which can be both the result of and facilitator of illicit flows.

To address and combat illegal cross-border flows, cross-country cooperation and coordination is needed to prevent, detect and sanction the corruption that contributes to the problem. Efforts have to look at specific interventions that can strengthen borders as well as broader governance issues that can help to build the transparency, accountability and integrity of institutions and key actors.

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## 1 Illegal Cross Border Flows and Corruption

Cross-border flows of funds, goods and services, and people involve multiple actors and countries that are often spread across the North and South. Illegal or illicit cross-border flows can plague sectors, such as the natural resource and the extractive industries, given the demand by markets for these goods (Leading Group 2007; Global Witness 2000, 2009).

Cross-border flows can also overlap, meaning that organisations are smuggling drugs in order to pay for the smuggling of guns to wage combat or insurgency. For example, the US State Department recently grouped the Taliban as one of the largest drug trafficking organisations in the world. At the same, cross border activities can fuel illicit flows that are internal to a country (and vice versa). In this case, the trafficking of persons within a country might generate funds that are used to back an illicit cross-border trade in other goods.

The interweaving of activities has been researched by the [UN Office on Drugs and Crime](#) (UNODC). It has released a paper on how transnational organised crime networks use fishing vessels to smuggle migrants, weapons, terrorists and wildlife (UNODC 2011).

Given the illicit nature of the transaction or movement, it is often difficult to obtain regional or global estimates to assess cross-border flows. Even the figures that have been calculated are believed to be on the low-end of the real problem (Reed and Fontana 2011).

Apart from the challenge of determining the scale, there is also no universal definition on what constitutes a cross-border illicit or illegal flow. For the purposes of this query, illegal or illicit flows will be looked at where:

- the movement itself is illegal;
- the flow (of money, goods and services) is the result of an illegal act; and/or
- the legal obligations relating to the flow (such as the payment of taxes) have not been respected (Reed and Fontana 2011).<sup>1</sup>

<sup>1</sup> In terms of legal obligations relating to a flow, namely tax evasion, it is either considered a crime or not in a country.

The examples cited in the query include cross-border flows that originate as the proceeds of crime (such as criminal activity, trade mispricing, corruption and tax evasion) or cross-border movements that involve illegal acts. The evidence provided is divided by type (i.e. funds, goods and services, and people) and country examples from the region are used (i.e. Bangladesh, India, Nepal and Pakistan). In this query, the flow of goods is broadened to include wild plants and animals.

### Funds

The best estimated figures on cross-border flows are for money. [Global Financial Integrity](#), one of the leading organisations analysing these movements, has calculated that illicit outflows from the developing world were approximately \$1.26 trillion in 2008 (Kar and Curcio 2011). In Asia, the flow of illicit funds has grown between 2000 and 2008 by nearly eight per cent a year. Overall, Asia accounts for 44.4 per cent of total illicit flows from the developing world.

The countries in the region with the largest annual average monetary outflow for this period are as follow (Global Financial Integrity 2010):

	Country	Amount Millions of US\$
1	China, P.R.: Mainland	241.777
2	Malaysia	32.369
3	Philippines	12.142
4	Indonesia	11.608
5	India	11.569
6	Thailand	5.140
7	Brunei Darussalam	3.488
8	Bangladesh	1.581
9	Nepal	563
10	Lao People's Dem. Rep.	333
11	Myanmar	317
12	Cambodia	263
13	Maldives	143
14	Mongolia	116
15	Papua New Guinea	89
16	Samoa	38
17	Solomon Islands	27

India, which falls high on the regional list, sees significant inflows and outflows of illicit capital (mostly through balance of payments but also through trade mispricing). Further research done on [India](#) suggests

that it has lost more than US\$ 460 billion since 1948 after the country won its independence. Poor governance has been cited as one of the sources for these flows (Kar 2010). Illicit outflows from India also capture processes that rely on corruption to function, such as money laundering. According to the Financial Action Task Force (FATF), the main sources of money laundering in India are the result of illicit activities that include drug trafficking, fraud, organised corruption, human trafficking and corrupt acts (such as bribery and kickbacks; FATF 2010).

### Goods and Services

The illegal cross-border movement of goods and services is often termed “illicit trade”, which has been estimated by **Moises Naím**, an expert on the topic, to reach 10 per cent of the value of global commerce.

Illicit trade includes goods and services that are illegal (such as illicit logging and wildlife, drugs and arms) as well as those that are legal but which are moved across borders illegally (such as through the payment of bribes to circumvent customs and duty taxes). Essential goods (e.g. foodstuffs and fuel) and counterfeit products would fall within the category termed illicit trade. **US companies** alone have estimated that they lose between US\$ 200 and US \$ 250 billion in revenue due to illicit trade in counterfeited goods.

Documented goods and services that are being illicitly traded in Bangladesh, India, Nepal and Pakistan include arms, cigarettes, drugs, foodstuffs and wild plants and animals (see below). In many of these instances, as in other parts of **Asia**, transnational organised crime networks are behind the local trade.

### Arms

The **International Action Network on Small Arms** has estimated that the global illegal trade in small arms may reach US\$ 10 billion annually (Transparency International, 2008). Around the world there are thought to be a total of 75 million illegal small arms in circulation. **India** is believed to have around more than half of the worldwide total (Oxfam 2006).

Many of these weapons have found their way into India through the border that the country shares with Nepal. It has been alleged that these arms are being used by **insurgent groups** within India. Another weak area in India is its border with Myanmar, which forms part of the **Golden Triangle** area known for arms and drug trafficking. As with other countries, in India these trades

often overlap and are controlled by groups that use the illicit trade in drugs to purchase weapons. While there is no documentation of corruption being used to allow these movements, it is thought that corruption among law enforcement and customs agents may be facilitating the problem (see below).

Weak border controls contribute to the illegal flow of arms among other countries in the region, including Afghanistan and Pakistan. In **Pakistan**, it has been alleged that illegal arms factories set up near the border are furnishing the fire power needed to help the Taliban's insurgency in Afghanistan (as well as to pursue attacks in Pakistan). It has been well-documented that arms and other illicit flows are crossing Pakistan's border and helping to equip the Taliban and other fringe insurgent groups (UNODC 2010; Felbab-Brown 2010).

Yet the illicit arms trade is not only fuelled by small producers. Arms traders are thought to spread the problem broader, buying up equipment from countries coming out of recent conflicts (such as Cambodia) to sell to buyers seeking to pursue new violence or fuel prolonged conflicts, such as in Sri Lanka, India, Myanmar, Nepal and the Philippines (Florquin 2006).

### Cigarettes

Within the illicit cigarette trade, India and Pakistan stand out globally as being among the top ten countries involved; they are respectively numbers seven and nine on the list (Joossens et al 2009).

It is estimated that nearly 12 per cent of the global cigarette market is illicit, causing a loss of US\$ 40.5 billion in revenue each year. In India, the share of the total illicit cigarette market is 14 per cent (Joossens et al 2009). In Pakistan, the share is higher at 18 per cent, of which 5 per cent is thought to be caused by smuggling and 13 per cent through illicit manufacturing (Baloch and Khoso no date).

According to a four-country study (Bangladesh, India, Pakistan and Sri Lanka) in South Asia, corruption and the involvement of law enforcement agencies were documented as facilitating the illicit cigarette trade (Kabir et al 2010). The linkage between police and smugglers ranged from apathy to active support, through the acceptance of bribes. There was also a clear linkage between wealthy and powerful political actors and the smugglers in all of the countries. Such connections left law enforcement authorities with little power to combat the problem. Specific instances in

corruption at the border between India and Nepal were documented.

### Drugs

Given the nature of the drug trade, there are very few numbers available on its overall value. The problem is currently assessed based on shipments that are interdicted (weighed in tons), their estimated “street value” and the routes used.

In Asia, one of the focal points of the problem is Afghanistan (the other key one is Myanmar). Afghanistan is the source of **90 per cent of the world’s opium**, which is processed into heroin worth US\$ 55 billion. **Afghanistan** is also the world’s number one producer of cannabis resin. It is estimated by the United Nations that 40 per cent of Afghanistan’s heroin and morphine transits through or is consumed in its neighbour, Pakistan (UNODC 2010). A serious challenge for Pakistan is its 2,430 km-long, porous border with the country. Heroin from Afghanistan has also been documented in transit through India and other countries of the Arabian Peninsula to markets in Africa (UNODC 2010).

According to the UNODC, there are two ways that drug trafficking poses a threat to the governance of countries. First, it allows the funding of illegal armed groups and permits a flow of money to corrupt and/or confront the state (UNODC 2010). Second, drug traffickers tend to collude and corrupt legitimate state institutions, infiltrating government and facilitating state capture (Chene 2008). In the process, instability and insecurity can arise and the state may become “captured” by these interests rather than functioning for the public good.

### Wild Plants and Animals

There is a flourishing trade in wild plants and animals that generates globally an estimated US \$6 billion dollars per year (Transparency International, 2007). While there is a global agreement to prevent this commerce — the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES) — poachers and other criminal groups have set up elaborate international networks that take advantage of a black market trade. A **British investigation** into one of these networks has shown the extent of their reach, linking countries in Asia and Africa to purchasers in Europe and the US.

**Transparency International** has tried to better understand how such networks function, particularly in terms of illegal logging. The organisation has documented the corruption linkages involved in the trade based on field work in South Asia that was conducted through the Forest Governance Integrity (FGI) project. FGI looks at how corruption contributes to illegal logging in supply (Indonesia, Papua New Guinea and the Solomon Islands), transit (Malaysia) and demand countries (China). The cross-border nature of the trade is facilitated by different drivers of corruption, including: political corruption, foreign bribery in supply countries, corruption in licensing and concessions, timber ‘laundering networks’, judicial corruption and weak due diligence on the part of financial institutions. The project has produced a **manual** on how to identify these different risks along the timber supply chain.

In Nepal, the **World Wildlife Fund** has looked at similar factors that have made the country an international transit stop for poached animals, a trade which is allegedly being financed by groups linked to global criminal networks. Wildlife parts and derivatives are seen as passing through Nepal from other supply countries (including China and India) as a result of the weak governance of the sector.

While Nepal is a signatory to CITES and has the legal and institutional mechanisms in place, the sophistication of the cross-border trade is beyond its capacity. WWF is trying to work with the Nepalese government to promote regional and international cooperation to mitigate the external drivers, including international demand and enforcement gaps (such as border police and customs).

### People

It is estimated by the **US State Department** that globally there are 12.3 million adults and children who have been trafficked and are being forced or bonded into labour and prostitution (US State Department 2010). According to the UNODC, Bangladesh, India, Nepal and Pakistan have a high incidence of human trafficking, serving as the countries of origins for the persons being moved within or across borders. Interestingly, India and Pakistan also are countries that receive a high level of trafficked persons (UNODC 2006). Police involvement is cited by many trafficking victims in these countries and corruption within the force is considered an endemic problem that is



facilitating the cross-border movement of people (Nair and Sen 2006).

### Bangladesh

In **Bangladesh**, there are no clear figures for the number of trafficked persons. However, it is estimated that between 10.000 and 20.000 women and children are trafficked every year from Bangladesh to India, Pakistan and countries such as Kuwait and the United Arab Emirates.

**Research** suggests that corruption plays a role in human trafficking through fraudulent work contracts and the use of bribery. Moreover, there are reports that there is a network of members of parliament, corrupt recruiting agencies and village level brokers that participate in the trafficking of Bangladeshis (US State Department 2010). There has also been documented collusion between traffickers and public officials at all levels (US State Department 2010).

### India

In **India**, figures suggest that women and children are heavily trafficked and forced into labour. It is estimated that more than 1.2 million children are trafficked, mostly as child prostitutes. **India's Home Secretary** has stated that trafficking-related activities involve up to 100 million Indians in roles such as middle-men, traders and employers.

A broad study that interviewed more than 852 government officials in India found that corruption in the police and the political ties that traffickers had were factors for the failure to take action in trafficking cases (Nair and Sen, 2006). About 15 per cent of the respondents cited weaknesses in the police and judiciary as preventing enforcement. Anecdotal evidence supports these results. For example, nearly one-fourth of the 540 members of India's Parliament face charges for crimes such as human trafficking and immigration scams (Global Integrity 2009a).

### Nepal

Numbers of trafficked Nepalis are considered difficult to determine. However, it is estimated that three million Nepalis have gone to other countries for work (not including India), as a result of legal and illegal channels (US State Department 2010). For Nepalis, India remains the top destination for workers — who are trafficked or arrive willingly (US State Department 2010).

In **Nepal**, law enforcement officials believe that the trafficking of people increasingly is controlled by well-organised syndicates that are linked to other illicit trades, such as drug trafficking (US State Department 2010). There is also evidence of the kidnapping of Nepali girls by such networks to work in the sex trade in India (Shamim 2001).

### Pakistan

It is estimated that there are 1.7 million trafficked persons living in **Pakistan**. Other estimates suggest that there are between 15-20 million Pakistanis who have been affected by trafficking.<sup>2</sup>

An **ILO report** on forced labour found contract fraud occurring among some Pakistani temporary contract workers that had been recruited to take positions in Persian Gulf states.<sup>3</sup> Further evidence suggests that there are networks of powerful individuals who are involved in trafficking and who have political connections that help to keep them in business (US State Department 2010).

## 2 Linkages between corruption and cross-border illicit flows

As the above examples demonstrate, cross-border corruption provides the entry point needed for the illegal movement of funds, drugs, arms and people between countries (Johnston 1997). Corruption is also seen as the medium that facilitates these cross-border flows (Shelley 2010), particularly given the weaknesses that corruption poses for managing borders (Seniora and Poitevin 2010).

As might be expected, countries with cross-border problems of corruption and illicit flows are also those that generally have problems with domestic corruption

<sup>2</sup> These figures are based on the Human Rights Commission of Pakistan State of Human Rights in 2005 (2005), pg. 230 and Human Rights Commission of Pakistan State of Human Rights in 2004 (2004), pg. 218. See: <http://www.hrcp-web.org/archive.html>. Transparency International is producing a forthcoming working paper on the linkages between corruption and human trafficking.

<sup>3</sup> Either a new contract was issued when they arrived or the original contract had new terms and conditions (and was not understandable). In some cases, the new contract reduced the wages that were guaranteed by 10 per cent.

(Johnston 1997). These same countries are vulnerable to outside influences, including illicit networks (Johnston 1997; Leading Group 2008). Evidence suggests that illicit networks that are driving the illegal flow of money, goods and services, and people are intrinsically linked to large-scale corruption in the countries that are serving as supply, demand and transit countries (Reed and Fontana 2011).

This linkage has been empirically proven through studies that have looked at the relationship between the growth of criminal networks and public sector corruption (Buscaglia 2003). Among the findings, it was highlighted that countries are less vulnerable to corruption and organised crime when they have strong justice systems, and integrity and independence characterise the judiciaries. Moreover, organised crime was more prevalent in countries where the rule of law was weak, further undermining domestic institutions in the public and private sectors (Chene 2008).

In terms of Bangladesh, India, Nepal and Pakistan, different surveys and studies have found these four countries to have significant problems related to public sector corruption and governance breakdowns that would make them vulnerable to cross-border flows:

- **Bangladesh:** According to Transparency International's 2010 **Corruption Perceptions Index (CPI)**, the country is ranked number 25 out of 33 countries in the region (with number one being the best and number 33 being the worst). Based on the **Global Integrity Index** (2008), Bangladesh is seen to have a weak level of integrity due to the poor implementation of the current legal framework, signalling the problem of enforcement. According to TI's **Global Corruption Barometer** 2010, the institution that is perceived to be the most corrupt in the country is the one tasked with law enforcement: the police.
- **India:** India is ranked number 16 in the Asia Pacific (and 87 overall) on the CPI from 2010. Findings from **Global Integrity** (2009a) suggest that the country has severe integrity gaps, particularly when it comes to political financing, judicial accountability and law enforcement. The results of this problem are seen in the public's perception of related institutions. Based on TI's **Global Corruption Barometer** from 2010, political parties, the police and parliament are considered the most affected by corruption.

- **Nepal:** The findings of the CPI 2010 show that the country is ranked the worst among the four countries on public sector corruption, both regionally and globally. According to the results of the 2009 **Global Integrity Index**, Nepal has anti-corruption integrity promoting policies on the books but there are very large gaps in their implementation. One direct impact of these problems is the country's inability to control cross-border flows. There are several allegations of corruption being pervasive among government officials working in customs and immigrations (Global Integrity 2009b).
- **Pakistan:** The country falls in at number 27 in the region (and 143 overall) based on the CPI 2010. Of those surveyed as part of TI's Global Corruption Barometer 2010, 77 per cent of Pakistanis responded that corruption has worsened there in the last three years. The same survey shows that the public views the police as the institution most affected by corruption in the country. A **Global Integrity report** (2008) signals related challenges due to a huge gap in the implementation of the country's legal framework. The country has many of the traits of an ungovernable country and is ranked number ten on the **Failed States Index** (2009).

When countries have such challenges with corruption and governance, outside forces can easily take advantage of rent-seeking individuals within the country. These individuals engage in corrupt activities that spill across borders and cause corruption to worsen domestically while allowing the corrosive influences of outside forces to take root, creating a vicious cycle.

The interplay between internal and external forces often occurs at the border but extends beyond it. Smugglers or middlemen may bribe officials, usually in customs or in related ministries, to allow their transport to continue across borders. However, such payments are symptoms of a more serious and broader problem that involves chains of actors who form transnational networks that are linked through corruption. Corruption brings criminal networks together at different levels (Transparency International 2008). Corruption networks have been well-documented in other regions, such as the South Caucasus (Mirimanova and Klein 2006). This can create a situation where corruption in one area — the illicit network — “feeds” off the corruption in government (Klein 2007).

Such a situation has been documented for Nepal and India along their borders. Here a void in governance, due to weak border controls and corruption among civil servants, is alleged to have facilitated a network of black market traders, operating in goods from ghee (a type of butter) to cell phone SIM cards. This trade is allegedly used to support militant groups in other countries, including Pakistan. Research shows that these illicit networks are using laundering techniques to exploit long-existing gaps in Nepal's legal framework and anti-corruption systems (Miklian 2009). It also is alleged that bribes in Nepal are often paid right from the start when a customs agent begins his or her duty. For example, a Nepali customs official who wants placement on the border patrol must bribe someone in government to get the position, who then must continue to provide kickbacks to this government benefactor back in the capital (Miklian 2009).

A similar problem of networks feeding corruption has allegedly been created along the borders of **Pakistan**. The country's interior minister Rehman Malik has publicly stated that corrupt officials are helping human and drug traffickers ply their trade, which in turn is benefitting militant groups in the country. At the same time, this trade is also viewed as feeding corruption in the country (Shelly and Hussain 2009). The specific features of the border area between Pakistan and Afghanistan have aggravated the problem. The border is an extremely volatile area and one where corruption and violence spill across the countries. Apart from armed groups and organised criminal networks, it has been alleged that law enforcement and public officials are earning millions of dollars by running their own illegal trade. This includes an illegal food trade in the Punjab province that is smuggling wheat and flour for sale in Afghanistan (Global Financial Integrity 2008).

### 3 Conclusion

Cross-country cooperation and coordination are demanded to prevent, detect and sanction the corruption that is feeding illegal cross-border flows. It also means recognising how the movements of funds, goods and services, and people are facilitating cross-border corruption.

Policy approaches to illicit flows (of money, goods and services, and people) have been principally pursued through initiatives targeting the money trail, namely anti-money laundering legislation, as well as the source

of the flows, such as anti-human trafficking laws and strict plant and wildlife regulations.

This work has mostly been done by ensuring that national laws are consistent with regionally and globally-agreed legal frameworks on corruption, trafficking and other areas. Except for India, all the countries included in the query have ratified the UN Convention Against Corruption (UNCAC). Other key global agreements that are used as a reference point include the **UN Convention against Transnational Organised Crime, CITES** (on wildlife and plants) and the **Palermo Protocol** (on human trafficking).<sup>4</sup> As has been seen in practice, what is essential for any of these conventions to be effective is their active enforcement and implementation.

At the same time, specific actions have been taken by countries to address the overt governance breakdowns and corruption risks along borders. Efforts include training for police and customs officials on ethics and corruption, the establishment of whistleblower mechanisms and protections, joint patrols, and salary adjustments to mitigate the incentive for civil servants working along the border to accept bribes (Miklian 2009).

However, there is an increasing shift towards measures that look for up-stream solutions, such as good governance promotion and institutional capacity building to serve as a bulwark against corruption and, in turn, against the generation of illicit flows (Reed and Fontana 2011). For example, such an approach would look at how to strengthen law enforcement bodies (i.e. the police and judiciary), banking regulations (i.e. due diligence and 'know your customer') as well as how to ensure that political parties have transparent funding (i.e. to prevent their cooption and financing by transnational networks).

All of these examples suggest that effective remedies should function within a broader universe of policies that can deal with the overlapping-nature of the problem of cross-border corruption and illicit flows. Rather than single interventions, they should be complementary and reinforce each other.

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<sup>4</sup> The Palermo Protocol is a supplement to the UNTOC and was approved in 2000.

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