

Basel AML Index 2016 Report

Basel Institute on Governance | 27 July 2016

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1 Introduction

This report is issued on the occasion of the launch of the fifth edition of the Basel Anti-Money Laundering (AML) Index which has been published by the Basel Institute on Governance (Basel Institute) since 2012. To date, the Basel AML Index remains the only index published by an independent not-for-profit organisation ranking countries according to their risk of money laundering and terrorist financing. The Basel AML Index is used by the private sector as an established AML country risk-rating tool for compliance purposes, and in the public sector for research and policy measurement.

The Basel AML Index 2016 edition covers 149 countries and provides risk ratings based on the quality of a country's framework for AML and countering terrorism financing (AML/CFT) and related factors such as perceived levels of corruption, financial sector standards and public transparency.

The results of the Basel AML Index, which are presented in chapter 3, are derived from 14 indicators using publicly available sources such as the FATF, Transparency International, the World Bank and the World Economic Forum. The scores are aggregated as a composite index using a qualitative and expert-based assessment. An analysis of the results of the 2016 edition of the Basel AML Index is presented in chapter 4.

It is important to read these results chapters in conjunction with chapters 2 and 5, which provide a detailed account of the scope of what the AML Index can and cannot measure, and the methodology used to calculate the overall score of the Basel AML Index. Without this background, results of composite indices may easily be misunderstood or misrepresented, and this may have unwanted consequences on any policy or compliance decision that is taken as a result of using the AML Index. The Basel Institute has conducted extensive research in calculating the final results following academic best practices, and has its methodology reviewed and validated by an international and independent panel of peer reviewers. The panel also checks that the rating is accurate, plausible and continues to capture the latest development in the area of AML/CFT risks. A report from the 2015 peer review exercise is included in this report in chapter 6.

The Basel AML Index is offered in two editions: The Public Edition offers the annual ranking of countries according to their risk profiles and is available free of charge. The Expert Edition provides a more comprehensive data set and allows for a selection of individual sub-indicator of the Index. The Expert Edition is also periodically updated, covers some 50 countries more than the Public Edition, and includes sanctions lists. With these additional features, it can serve as a sophisticated country risk assessment tool for regulatory purposes, particularly for compliance officers, and caters to users' diverse needs in relation to different compliance and regulatory requirements. The subscription-based Expert Edition is also offered free of charge for public, academic and non-profit organisations; commercial enterprises are charged an annual fee starting at CHF 2000 depending on user intensity. Further details concerning the Expert Edition are described in chapter 7.






















































































































































The Basel Institute continues to actively facilitate the exchange of knowledge on the challenges of AML/CFT risk rating. We therefore encourage comments and feedback on the Basel AML Index, as we strive to advance the use of AML country risk ratings for both research and compliance purposes.

2 What does the Basel AML Index measure?

The Basel AML Index measures the risk of money laundering and terrorist financing of countries based on publicly available sources. A total of 14 indicators dealing with AML/CFT regulations, corruption, financial standards, political disclosure and rule of law are aggregated into one overall risk score. By combining these various data sources, the overall risk score represents a holistic assessment addressing structural as well as functional elements in the AML/CFT framework. As there are no reliable quantitative data on money laundering available, the Basel AML Index does not measure the actual existence of money laundering activity or amount of illicit financial money within a country but is designed to indicate the risk level, i.e. the vulnerabilities of money laundering and terrorist financing within a country.

The Basel AML Index ranks countries based on the overall score and provides data that is useful for comparative purposes. However, it should be stressed that the primary objective is not to rank countries in comparison to each other. Rather, the Basel AML Index seeks to provide an overall picture of a country's risk level and to serve as a solid starting point for examining progress over time.

3 Basel AML Index 2016 Scores and Rankings

1		Iran	8.61	51		Algeria	6.50	101		Uzbekistan	5.10
2		Afghanistan	8.51	52		Guyana	6.48	102		Albania	5.04
3		Tajikistan	8.19	53		Cote D'ivoire	6.42	103		France	5.03
4		Uganda	8.01	54		Bangladesh	6.40	104		Austria	5.02
5		Guinea-Bissau	7.99	55		Philippines	6.31	105		Canada	5.00
6		Cambodia	7.89	56		Brazil	6.23	106		Australia	4.99
7		Mozambique	7.89	57		Indonesia	6.23	107		Netherlands	4.99
8		Mali	7.86	58		Russia	6.22	108		Macedonia	4.98
9		Sudan	7.85	59		Ghana	6.22	109		Spain	4.94
10		Myanmar	7.71	60		Kyrgyzstan	6.21	110		Korea, South	4.92
11		Kenya	7.71	61		Mongolia	6.11	111		Singapore	4.91
12		Nepal	7.57	62		Papua New Guinea	6.11	112		Latvia	4.91
13		Guinea	7.55	63		Honduras	6.04	113		Qatar	4.90
14		Paraguay	7.44	64		Seychelles	6.00	114		Israel	4.89
15		Liberia	7.41	65		United Arab Emirates	5.98	115		Jordan	4.88
16		Laos	7.40	66		Guatemala	5.97	116		Slovakia	4.88
17		Sao Tome And Principe	7.33	67		Botswana	5.95	117		South Africa	4.86
18		Zambia	7.32	68		Costa Rica	5.93	118		Azerbaijan	4.84
19		Haiti	7.32	69		Trinidad And Tobago	5.92	119		Montenegro	4.82
20		Bolivia	7.29	70		Luxembourg	5.89	120		Chile	4.80
21		Lesotho	7.24	71		Kazakhstan	5.88	121		United Kingdom	4.77
22		Burkina Faso	7.21	72		Timor-Leste (east Timor)	5.87	122		Egypt	4.74
23		Sri Lanka	7.16	73		Nicaragua	5.84	123		Georgia	4.71
24		Sierra Leone	7.12	74		Mauritius	5.82	124		El Salvador	4.69
25		Panama	7.09	75		Serbia	5.82	125		Czech Republic	4.66
26		Ethiopia	7.09	76		Japan	5.76	126		Belgium	4.65
27		Tanzania	7.08	77		Malawi	5.76	127		Norway	4.63
28		Lebanon	7.02	78		India	5.69	128		Armenia	4.63
29		Vanuatu	7.01	79		Mexico	5.60	129		Tunisia	4.62
30		Niger	6.98	80		Morocco	5.59	130		Colombia	4.55
31		Zimbabwe	6.98	81		St. Vincent And The Grenadines	5.59	131		Ireland	4.54
32		Nigeria	6.97	82		Bahrain	5.59	132		Malta	4.49
33		Mauritania	6.82	83		Kuwait	5.54	133		Iceland	4.47
34		Argentina	6.74	84		Greece	5.53	134		Romania	4.46
35		Cape Verde	6.74	85		Hong Kong Sar, China	5.51	135		Poland	4.40
36		Dominican Republic	6.74	86		Ecuador	5.48	136		Dominica	4.40
37		Angola	6.71	87		Malaysia	5.46	137		Sweden	4.32
38		Rwanda	6.70	88		Switzerland	5.46	138		Peru	4.31
39		China	6.70	89		Senegal	5.37	139		Portugal	4.21
40		Yemen	6.69	90		Italy	5.36	140		Jamaica	4.16
41		Marshall Islands	6.67	91		Saudi Arabia	5.34	141		Croatia	4.15
42		Gambia	6.67	92		Germany	5.33	142		Hungary	4.15
43		Vietnam	6.67	93		Moldova	5.24	143		Denmark	4.08
44		Namibia	6.64	94		Bosnia-Herzegovina	5.18	144		Slovenia	4.06
45		Pakistan	6.62	95		Grenada	5.18	145		New Zealand	3.86
46		Ukraine	6.57	96		St. Lucia	5.17	146		Bulgaria	3.83
47		Turkey	6.55	97		United States	5.17	147		Estonia	3.82
48		Venezuela	6.53	98		Uruguay	5.15	148		Lithuania	3.62
49		Thailand	6.52	99		Taiwan, China	5.12	149		Finland	3.05
50		Benin	6.52	100		Cyprus	5.12				

4 Results & Findings

4.1 High risk countries

The 10 highest risk countries in the 2016 Basel AML Index are Iran, Afghanistan, Tajikistan, Guinea-Bissau, Cambodia, Mozambique, Mali, Sudan, Uganda and Myanmar. Although overall this list has changed very little from the previous edition, it is noteworthy that Guinea-Bissau and Mali have seen some improvement in their scores. The majority of the higher risk countries however, have only slightly changed their risk rating, indicating slow progress and difficulties in conducting structural changes that could improve their AML/CFT framework.

Low-income and sub-Saharan countries have a proportionally high presence in the top third of the highest risk countries of the Basel AML Index. The data shows that these countries were assessed as having weak AML/CFT systems combined with structural and functional vulnerabilities such as high rates of perceived corruption, weak judicial systems and inadequate financial sector standards. It is important however to note that the fact that these countries are placed higher in the risk-rating category does not necessarily mean that they can automatically be considered as attractive destinations for money launderers. It only means that the country has a heightened vulnerability to money laundering due to shortcomings in their AML systems as assessed by international standards. More on this is explained in the methodology chapter.

Country	Overall Score
Iran	8.61
Afghanistan	8.51
Tajikistan	8.19
Uganda	8.01
Guinea-Bissau	7.99
Cambodia	7.89
Mozambique	7.89
Mali	7.86
Sudan	7.85
Myanmar	7.71

Table 1 – Top 10 High risk countries

While it is the overall deficiencies in a country’s AML/CFT framework that weigh most heavily on the result, the final score is made up of a combination of factors, including structural deficiencies noted above, as well as the size of a country’s financial centre or its potential attractiveness as destination country for illicit financial flows. See figure 1 for an illustration of this.

What leads to high risk in the Basel AML Index?

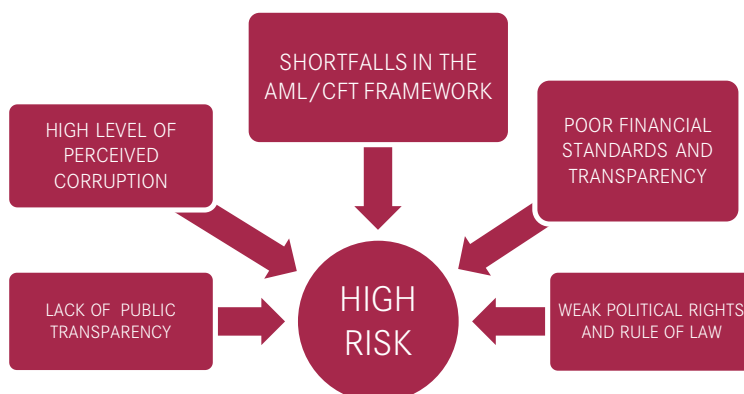


Figure 1 - What leads to high risk in the Basel AML Index?

4.2 Low risk countries

Finland remains the lowest risk country in the Basel AML Index but Estonia lost its ranking as the second lowest risk country due to a significantly worsened score, up from 3.19 in 2015 to 3.82 this year. Lithuania has taken Estonia’s place as second lowest risk country in the 2016 ranking. Among the low risk countries, Slovenia has also seen its score worsen significantly, from 3.41 last year to 4.06 in 2016.

Country	Overall Score
Finland	3.05
Lithuania	3.62

Table 2 - Low risk countries

Most countries grouped near the lower risk category can demonstrate a strong AML/CFT compliance level. Additionally, they portray high public and financial transparency and low levels of corruption. Some of these countries are also positively influenced in comparison to other countries because they are not considered a significant financial centre and play a smaller role in the global economy.

For a majority of countries with lower risk ratings, their positive ranking derives importantly from the FATF Mutual Evaluation Report (MER). However, this and last year’s Basel AML Index show that the revised FATF methodology, which focuses on the effective implementation of countries’ AML/CTF framework, tends to result in less favourable rating in a number of countries, because the actual implementation of laws seems to lag behind technical compliance. Belgium and Italy for example, despite improving their legal frameworks, received due to the evaluation of its effectiveness a worse overall assessment compared to their previous assessments. It can be expected that the scores of some of the lower risk countries might worsen in the coming years as the revised FATF methodology is applied in more countries. At this point, however, the majority of countries are still rated according to the old FATF methodology only.¹

4.3 Largest improvements and deteriorations

Top 10 improvers 2016

Country	Overall Score 2016	Overall Score 2015	Change in score 2015-2016
Kuwait	5.54	6.25	↑ -0.71
Ecuador	5.48	6.05	↑ -0.57
Seychelles	6.00	6.53	↑ -0.53
Albania	5.04	5.56	↑ -0.52
Bosnia-Herzegovina	5.18	5.64	↑ -0.46
Austria	5.02	5.45	↑ -0.43
Costa Rica *	5.93	6.34	↑ -0.41
Greece	5.53	5.83	↑ -0.30
Korea, South	4.92	5.2	↑ -0.28
Armenia *	4.63	4.89	↑ -0.26

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

Kuwait has addressed a number of key deficiencies pertaining to the FATF recommendations as attested by the FATF-Follow up report, which lead to the greatest improvement from the previous 2015

¹ See chapter 6.2 for more details on the use of the new FATF MERs in the calculation of the Basel AML Index.

edition.² The FATF the report also noted however that there is insufficient information to assess the effectiveness of the AML/CFT system, which will be evaluated in the next assessment cycle of the FATF.

Ecuador saw strong gains in the Public Transparency and Rule of Law indicators and Seychelles performed better in the Financial Secrecy Index (FSI) enabling it to lower its risk rating in the Basel AML Index. Albania, Armenia, Bosnia, and Costa Rica also improved due to recent re-evaluation of their AML/CFT legal framework under the FATF assessments, which rated their compliance levels more positively.

Austria's positive change was driven by improvements in the political finance indicator illustrating more transparency in relation to the financing of political parties and candidates; however Austria has also undergone an evaluation under the new FATF evaluation methodology, expected to be published in August 2016, which may change their rating again.

Greece and Korea improved as a result of the latest release from the FSI. Korea additionally improved in financial standards and public transparency.

Top 10 losers 2016

Country	Overall Score 2016	Overall Score 2015	Change in score 2015 - 2016
Vanuatu *	7.01	6.19	↓ +0.82
Chile	4.80	4.02	↓ +0.78
Sri Lanka *	7.16	6.44	↓ +0.72
Slovenia	4.06	3.41	↓ +0.65
China	6.70	6.05	↓ +0.65
Estonia	3.82	3.19	↓ +0.63
Serbia *	5.82	5.2	↓ +0.62
Turkey	6.55	5.93	↓ +0.62
Finland	3.05	2.53	↓ +0.52
Macedonia	4.98	4.5	↓ +0.48

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

Serbia, Sri Lanka and Vanuatu recorded a higher risk rating this year due to the new assessment methodology adopted by the FATF, which also assessed the effectiveness of their AML/CFT framework as mentioned above. The rankings of China, Estonia, Finland, Macedonia and Turkey deteriorated simply due to the fact that they were all included in the FSI for the first time and thus assessed according to their financial secrecy standards and their roles as financial centres. Chile's increase of its risk score was a combination of being included in the FSI and an increase in the perception of corruption from Transparency International (TI).

² MENAFATF Follow up Report on Kuwait, 2015: http://www.menafatf.org/MER/Kuwait_Exit_FUR_ENG.pdf (last accessed in June 2016)

Top 10 higher risk countries among OECD

Country	Overall Score
Luxembourg	5.89
Japan	5.76
Greece	5.53
Switzerland	5.46
Italy *	5.36
Germany	5.33
United States	5.17
France	5.03
Austria	5.02
Canada	5.00

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

EU Countries

Country	Overall score
Luxembourg	5.89
Greece	5.53
Italy *	5.36
Germany	5.33
Cyprus	5.12
France	5.03
Austria	5.02
Netherlands	4.99
Spain *	4.94
Latvia	4.91
Slovakia	4.88
United Kingdom	4.77
Czech Republic	4.66
Belgium *	4.65
Ireland	4.54
Malta	4.49
Romania	4.46
Poland	4.40
Sweden	4.32
Portugal	4.21
Croatia	4.15
Hungary	4.15
Denmark	4.08
Slovenia	4.06
Bulgaria	3.83
Estonia	3.82
Lithuania	3.62
Finland	3.05

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

4.4 Regional results

Top 14 higher risk in Europe & Central Asia

Country	Overall Score
Tajikistan	8.19
Ukraine	6.57
Turkey	6.55
Russia	6.22
Kyrgyzstan	6.21
Luxembourg	5.89
Kazakhstan	5.88
Serbia *	5.82
Greece	5.53
Switzerland	5.46
Italy *	5.36
Germany	5.33
Moldova	5.24
Bosnia-Herzegovina	5.18

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

Middle East & North Africa

Country	Overall Score
Iran	8.61
Lebanon	7.02
Yemen	6.69
Algeria	6.50
United Arab Emirates	5.98
Morocco	5.59
Bahrain	5.59
Kuwait	5.54
Saudi Arabia	5.34
Qatar	4.90
Israel	4.89
Jordan	4.88
Egypt	4.74
Tunisia	4.62
Malta	4.49

Latin America & the Caribbean

Country	Overall Score
Paraguay	7.44
Haiti	7.32
Bolivia	7.29
Panama	7.09
Argentina	6.74
Dominican Republic	6.74
Venezuela	6.53
Guyana	6.48
Brazil	6.23
Honduras	6.04
Guatemala	5.97
Costa Rica *	5.93
Trinidad And Tobago *	5.92
Nicaragua	5.84
Mexico	5.60
St. Vincent And The Grenadines	5.59
Ecuador	5.48
Grenada	5.18
St. Lucia	5.17
Uruguay	5.15
Chile	4.80
El Salvador	4.69
Colombia	4.55
Dominica	4.40
Peru	4.31
Jamaica	4.16

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

East Asia & Pacific

Country	Overall Score
Cambodia	7.89
Myanmar	7.71
Laos	7.40
Vanuatu *	7.01
China	6.70
Marshall Islands	6.67
Vietnam	6.67
Thailand	6.52
Philippines	6.31
Indonesia	6.23
Mongolia	6.11
Papua New Guinea	6.11
Timor-Leste (East Timor)	5.87
Japan	5.76
Hong Kong Sar, China	5.51
Malaysia *	5.46
Taiwan, China	5.12
Australia *	4.99
Korea, South	4.92
Singapore	4.91
New Zealand	3.86

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

South Asia

Country	Overall Score
Afghanistan	8.51
Nepal	7.57
Sri Lanka *	7.16
Pakistan	6.62
Bangladesh	6.40
India	5.69

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

Sub-Saharan Africa

Country	Overall Score
Uganda *	8.01
Guinea-Bissau	7.99
Mozambique	7.89
Mali	7.86
Sudan	7.85
Kenya	7.71
Guinea	7.55
Liberia	7.41
Sao Tome And Principe	7.33
Zambia	7.32
Lesotho	7.24
Burkina Faso	7.21
Sierra Leone	7.12
Ethiopia *	7.09
Tanzania	7.08
Niger	6.98
Zimbabwe	6.98
Nigeria	6.97
Mauritania	6.82
Cape Verde	6.74
Angola	6.71
Rwanda	6.70
Gambia	6.67
Namibia	6.64
Benin	6.52
Cote D'ivoire	6.42
Ghana	6.22
Seychelles	6.00
Botswana	5.95
Mauritius	5.82
Malawi	5.76
Senegal	5.37
South Africa	4.86

* : Overall score based on a new FATF evaluation, which includes an effectiveness assessment.

4.5 Notes on the findings

The Basel AML Index scores provide an overall picture of a country's risk level and serve as a solid starting point for examining changes over time. While the Basel AML Index scores summarize a complex and multidimensional issue, they should not be viewed as an actual quantitative measurement of money laundering and terrorist financing activity, nor should they be taken as a specific policy recommendation for countries or institutions. For a detailed country diagnostic, the Basel AML Index should be complemented by a more fine-grained country profile study. Researchers, policy-makers and compliance officers who are interested in better understanding a country's risk rating/result are encouraged to consult the specific sub-indicators employed in the compilation of the Basel AML Index. The sub-indicators provide for each country a score that might be more relevant to a specific risk assessment such as for different client segments. A detailed view on the sub-indicators can be accessed via the Expert Edition. For more information on the Expert Edition see chapter 7.

5 Methodology

5.1 Methodological approach

The objective of the Basel AML Index is to provide a risk rating and not to measure money laundering itself as there is no reliable data to assess this, but to provide ranking countries according to their risk of money laundering and terrorist financing. This presents several methodological challenges. To date there has been no universally agreed definition or methodological approach that prescribes whether a particular country represents a high risk. Experts and regulatory institutions may have different requirements on the best method of assessing a country's risk. To address these challenges the Basel Institute conducted extensive research and created a conceptual framework to be considered for assessing money laundering and terrorist financing risk. In developing the Basel AML Index, a simplified approach, as prescribed in the best practices of creating a composite indicator³, has been used.

Figure 2 provides an overview of the steps that are being conducted to develop the Basel AML Index overall score.

Methodological overview

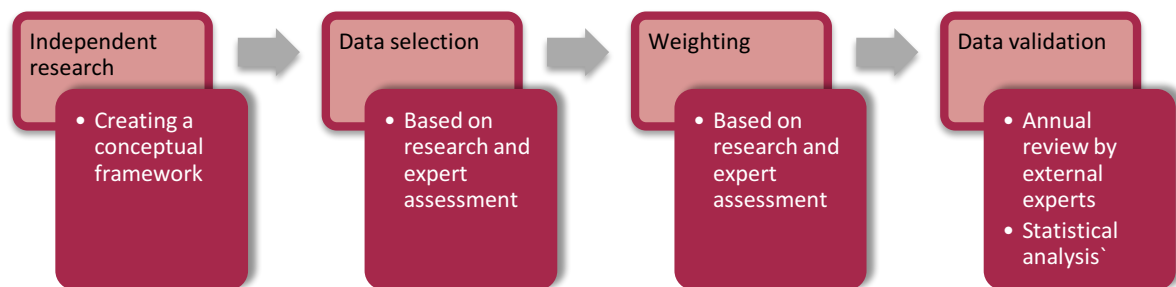


Figure 2 - Methodological overview

In sum, the development and conceptual framework of the Basel AML Index model is characterised by:

- A scientific approach in its creation (using the OECD composite index guidelines)
- Research and expert based selection of indicators
- A transparent annual review testing and validating its methodology and results with external experts from the AML community

³

Handbook on constructing composite indicators: methodology and user guide, OECD, 2008: <http://www.oecd.org/els/soc/handbookonconstructingcompositeindicatorsmethodologyanduserguide.htm> (as of 18 July 2016).

5.2 How is the overall score calculated?

The Basel AML Index is a composite index. This entails that the overall score is a weighted average of 14 indicators. The Basel Institute does not generate its own data but relies on data from various publicly available sources such as the FATF, Transparency International, the World Bank and the World Economic Forum. The indicators are grouped into five categories, based on the selected indicators and the conceptual framework to capture the multidimensionality of data (see figure 2).

Overall Score	Money Laundering / Terrorist Financing Risk (65%)	FATF Recommendations (30%)
		TJN- Finance Secrecy Index (25%)
		US INCSR – Volume II on Money Laundering (10%)
	Corruption Risk (10%)	TI CPI – Perception of Public Corruption (10%)
	Financial Transparency & Standards (15%)	WB Doing Business – Business Disclosure (1.88%)
		WEF GCR – Strength of auditing & reporting (5.63%)
		WEF GCR – Regulation of securities (5.63%)
		WB IDA IRAI – Financial Sector (1.88%)
	Public Transparency & Accountability (5%)	Int. Idea – Political Finance Database (1.67%)
		IBP – Open Budget Index (1.67%)
		WB IDA IRAI – Transparency, Account & Corr. (1.67%)
	Political Risk (5%)	FH – Press Freedom & Freedom in the World (1.67%)
		WEF GCR – Institutional Strength (1.67%)
		WJP – Rule of Law (1.67%)

Figure 3 – Basel AML Index Overall Score (percentages rounded to two decimal digits)

5.3 Selection of data

The Basel AML Index attempts to capture the whole scope of money laundering and terrorist financing risk and therefore applies a holistic approach in selecting the relevant risk indicators. Although, there is no universally accepted list of indicators in assessing a country’s money laundering and terrorist financing risk, some guidance exists on what to look out for. A key consideration is whether a jurisdiction has an adequate AML/CFT framework in place. An increasing focus is on the effectiveness of the implementation of such a framework as addressed in the revised FATF methodology. Other factors include the level of corruption and rule of law. Additional factors such as financial and public transparency as well as a country’s global role in the financial system should be considered to assess the whole picture. The criteria for the selection and inclusion of indicators are:

- Relevance and relationship to risks of money laundering and terrorist financing (related survey questions or assessment of relevant financial standards and regulations)
- Methodology of sources

- Availability of recent data (maximum age of data is 3 years with the exception of FATF Mutual Evaluation Reports)
- Country coverage
- Public availability
- Low overlap with other indicators

Annex 1 contains a table of sources including their individual weightings.

5.4 Scaling

Most indicators chosen for the Basel AML Index have their own scoring system. The individual sources (raw data) are rescaled to run from 0 – 10 where 0 indicates the lowest risk level and 10 the highest risk level. In order to reach a unified coding system all raw data or individual indicator scores were collected and rescaled using the Min-Max method into a 0 – 10 system. Only after rescaling the data is the indicator then applied in our composite index.

5.5 Weighting/Aggregation

In creating a composite index, each indicator or component receives a weight to aggregate all scores into one overall score. A standard and comparatively simple system would consist of adding all indicators and weighting them equally.⁴ This assumes however that all indicators are equally relevant in the context of money laundering and terrorist financing. The Basel AML Index though resorts to a diverse set of indicators, each of them measuring a different issue. Consequently, certain indicators are more important than others in assessing money laundering and terrorism financing risk. The Basel Institute has been applying its own weighting scheme in order to reflect an appropriate overall score. These individual weightings were agreed upon by senior anti-money laundering experts from the Basel Institute and the International Centre for Asset Recovery (ICAR) and are annually reviewed by independent external experts.⁵ The Basel AML Index team is also in contact with regulatory and supervisory institutions that are subscribed to the Expert Edition to discuss the weighting scheme. During our review and feedback phase no major criticism was received to change the current weighting methodology.

⁴ Another method would be through statistical models, such as factor analysis and data development analysis. Weights are in this case chosen to reflect the statistical quality of the data. Statistically more reliable data with broad coverage are assigned with more weighting. The OECD Handbook on Composite Indicators states however that “this method could be biased towards the readily available indicators, penalising the information that is statistically more problematic to identify and measure” OECD Handbook on Constructing Composite Indicators: Methodology and User Guide, OECD (2008): <http://www.oecd.org/dataoecd/37/42/42495745.pdf>

⁵ This approach is also known as expert weighting scheme or so-called participatory method, where experts rank or categorize each of the identified indicators in terms of their degree and relative importance. For example, the FATF Mutual Evaluation Reports which deal specifically with the topic of AML/CFT have been weighted stronger than, for example, indicators reflecting the civil rights or political risk indices, which should be also factored in but in a less representative way.

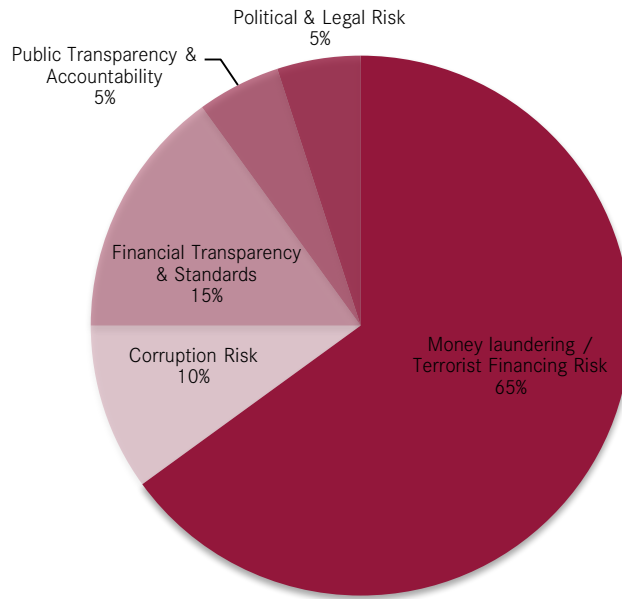


Figure 4 - Weighting scheme

5.6 Missing data / imputation of missing data

There is not always a complete set of 14 indicators available for all countries. Therefore, a country's overall score is calculated based on available data only, and missing values are not replaced. In the Public Edition of the 2016 Basel AML Index, only countries for which data is available for a minimum of 8 out of 14 indicators are included in the ranking. Countries for which data is missing in relation to all three indicators in the key category (ML/TF Risk) were excluded as well, regardless of whether in total data on 8 or more indicators was available for them.⁶ Applying these criteria, the 2016 version of the Public Edition of the Basel AML Index features 149 countries. By contrast, in the Expert Edition 203 countries are included, due to the inclusion of countries with less than eight indicators. These are specifically marked and indicated in the Expert Edition.

5.7 Data validation

As a final step, data is validated and cross-checked against a qualitative expert assessment and through an annual review. Each year a review meeting is conducted to assess the methodology anew and ensure that the country risk rating is being tested independently. The annual review meeting process entails verifying the quality of data/indicators and provides an additional layer of analysis to identify possible mistakes or inconsistencies within the ranking. The results of the annual review are published each year in the annual Basel AML Index report (see chapter 6 below), which allows for public scrutiny and verification by external experts, researchers and academics.

⁶ Due to our own weighting methodology the impact of certain missing indicator such as the ones within the ML/TF risk categories is higher than in other categories.

The 2014 annual review also included an internal statistical analysis to test the model, using for example a correlation analysis and testing the weighting scheme and comparing it with alternative weighting schemes. A summary can be read in the [Basel AML Index Report 2014](#).

6 Annual Review 2015

In order to provide a reliable risk ranking on AML/CFT, a regular quality check of the methodology and selection of indicators is for the Basel AML Index is essential. The Basel AML Index team assesses and tests the methodology and its country risk model outputs through a comprehensive annual review process based on external independent expert review.

Each year, the Basel AML Index team invites external experts from various backgrounds including the financial industry, law enforcement and dedicated international and non-profit organisations to participate in the annual review meeting to review the current Basel AML Index methodology and to provide feedback in order to ensure a transparent and participatory approach in calculating and validating the Basel AML Index.

The 2016 annual review meetings were held in Basel in the form of conference calls between 06 June and 13 June 2016. The talking points of the annual review meetings and any additional feedback received via emails as well as the decisions made based on these meetings, are summarised below.

6.1 General methodological approach and selection of indicators

During the annual review meetings, the Basel Institute provided a short overview of the methodological approach, stressing that the foundation for the development of the Basel AML Index lies in scientific research and its application for practical purposes as a compliance tool in conducting country risk assessments. Participants were asked to provide feedback on the methodology or share their views on it.

On the methodology and selection of indicators of the Basel AML Index, participants raised the issue of terrorism financing, which has garnered increased focus within the AML community, most notably at the FATF. Participants pointed out that money laundering and terrorism risk are two different aspects but combined within the same category in the Basel AML Index. While combining money laundering and terrorism financing risk as one category is not an issue, participants asked whether it would possible to identify which of the indicators within this category specifically cover terrorism financing.

In response to this, the Basel Institute referred to the use of the FATF Mutual Evaluation as the key indicator, which covers in their recommendation five to eight the elements of terrorism financing. The FATF scores provide an assessment of both the AML framework as well as the terrorism financing framework of each country. Due to the FATF scores being an aggregate of the forty recommendations, participants further inquired if it is possible to single out the individual recommendations assessing terrorism financing only. The Basel Institute proposed, if requested on an individual basis, to share the raw data of the FATF, which would allow users for individual assessment of each recommendation focusing on terrorism financing. Additionally, the Basel Institute informed the participants that the Expert Edition also covers the US State Sponsor of Terrorism list and marks countries according this list.

Participants referred to additional alternative sources such as the Terrorism Risk Index from Maplecroft, AEON Terrorism and Political Violence Risk Map and the Global Terrorism Index by the Institute of Economics and Peace.

Despite having given consideration to such indicators as well, the Basel Institute remains concerned regarding the use of such indicators in assessing terrorism financing. A limitation of these indicators is that they measure the level of incidents of terrorist activities or the number of mortalities caused by terrorism within jurisdictions without revealing reliable information regarding the financing of terrorism. Other participants shared these concerns as well. Given the lack of consistent data on terrorism financing, the Basel Institute will continue to monitor and review appropriate indicators that could provide better information on this topic. In case of new data being available, the Basel Institute shall make suggestions to include them for the next year's annual review.

6.2 Update on the new FATF Mutual Evaluation Reports (4th Round) incorporating the effectiveness rating

The FATF had originally developed 40 recommendations (published and revised in 1996). The FATF then updated its 40 recommendations in 2003 to include 9 Special Recommendations (regarding counter terrorist financing). The FATF recommendations were revised again in 2012 in order to merge the 40 + 9 Special recommendations into a total of 40 recommendations.

Since its inception, the Basel AML Index has been using the FATF Mutual Evaluation Reports (MER) and their table of compliance for assessing AML/CFT frameworks.

During this year's annual review, The Basel Institute provided a status update on its use of the MERs. As mentioned in last year's annual review, the Basel AML Index has been using the MERs and their table of compliance for assessing AML/CFT frameworks. The FATF assessment methodology rates the compliance with each recommendation on a four-tiered scale, from "compliant" to "largely compliant" to "partially compliant" to "non-compliant", which is translated into a numerical code in order to calculate an average score. Since 2015 the FATF has conducted and published thirteen MERs under a new assessment methodology, which combines an assessment of the FATF 40 Recommendations on the basis of technical compliance with an effectiveness assessment of the AML/CFT system. The Basel Institute has since then made use of the new FATF MERs and adjusted the methodology in order to provide a risk rating for countries assessed under the 4th round of FATF assessments covering the effectiveness measurement (see FATF table below):

FATF Mutual Evaluation Reports	FATF 40 Recommendation			FATF Effectiveness			FATF Technical + Effectiveness	
Country	Rec. 1	Rec. 2	...Rec. 40	Technical Compliance Average (standardised 0=low risk 10=high risk)	Effect.1	Effect.2	Effectiveness Average (standardised 0=low risk 10=high risk)	Basel AML Index - Weighted Average 1:2
Armenia	1	2	0	2.25	1	2	5.45	4.39
Australia	1	2	3	4.17	2	3	4.85	5.61
Belgium	2	2	2	3.33	2	2	5.45	4.75
Costa Rica	1	1	3	4.83	1	2	7.27	6.46
Cuba	2	3	2	2.33	1	1	5.15	4.21
Ethiopia	0	1	0	4.19	0	1	9.39	7.66
Italy	2	2	2	2.83	2	2	4.24	3.77
Malaysia	2	3	2	2.25	2	1	5.45	4.39
Norway	1	1	2	4.42	1	2	6.06	5.51
Samoa	1	1	2	5.08	1	2	7.27	6.54
Serbia	1	2	1	4.58	1	1	7.58	6.58
Spain	3	2	3	1.50	2	2	3.94	3.13
Sri Lanka	1	1	1	6.25	0	0	9.39	8.35
Trinidad & Tobago	1	2	2	3.75	1	1	8.18	6.70
Uganda	0	1	1	7.67	0	0	10.00	9.22
Vanuatu	0	0	0	6.83	0	0	10.00	8.94

Figure 5 - Use of the new FATF MER including effectiveness

Participants discussed the FATF’s new assessments methodology and the fact that the FATF does not assess countries annually on a regular cycle. Instead, countries are assessed one by one in infrequent cycles. The majority of countries’ FATF risk ratings are still based on the previous methodology without the effectiveness measurement. This means some countries are being assessed using different criteria and thus might be disadvantaged in the rating. The Basel Institute has already acknowledged the lack of comparability aspect in last year’s review but after consultation of external experts in the 2015 annual review meeting it was decided to include the new FATF assessment with the effectiveness measurement despite these limitations of comparability. The review group in 2015 considered the fact of having the most recent data available more important than the comparability aspect. During this year’s review, participants agreed and re-confirmed that it is necessary to include the latest FATF MERs but that a clearer indication should be made to those countries that were assessed under the new FATF methodology.

The Basel Institute will take up this suggestion and mark countries that have been assessed under the new FATF MER more prominently on the website.

6.3 Indicators for beneficial ownership information of trusts and companies

In light of the Panama Papers, aspects of transparency and beneficial ownership of companies and trusts has come under increased scrutiny. The Basel Institute conducted a preliminary assessment to determine whether requirements for the transparency and beneficial ownership of companies and trusts within jurisdictions are covered with the Basel AML Index. The Basel Institute found that by using the FATF MERs and the Financial Secrecy Index (FSI) developed by the Tax Justice Network, the Basel AML Index already sufficiently covers the risks associated with lack of beneficial ownership information, particularly in relation to the creation and use of trusts and companies. For example the FATF assesses countries' due diligence measures and efforts to prevent the misuse of legal persons when it comes to trust and company service providers in recommendations 22, 24 and 25. The FSI also assesses aspects of trusts and beneficial ownership of companies in one of their two components, namely the fifteen key financial secrecy indicators (KFSIs). Particularly the KFSIs two, three, and four used to assess jurisdictions are of particular relevance.⁷

The participants also felt that the indicators above sufficiently address the assessment of beneficial ownership information of companies and trusts. It was agreed that no further action is required on this topic.

In relation to the use of the FSI, one participant asked whether the FSI was assessed and checked for its methodology, as the organisation behind the FSI seem to have a certain political bias. Responding to this, the Basel Institute applies the same criteria for the selection of sources for all organisations, independent from any particular vision of any given organisation. All sources are subject to a quality control by the Basel Institute and the external review group through the annual review meetings. Additionally, an internal assessment has been conducted and concluded that FSI's approach is line with the criteria applied by the Basel Institute (see the [Basel AML Index Project Report 2013](#) for the summary of the annual review).

6.4 Risk levels

The Basel Institute encouraged discussion among participants in terms of breaking down the risk rating into various risk levels. The current scale of rating is from 0 (low risk) to 10 (high risk) and is broken down into three risk levels for illustration purposes:

- 0 - 3.3 (low risk),
- 3.3 - 6.6 (medium risk),
- 6.6 - 10 (high risk).

Participants were asked to review and share their own experience and approaches in categorising countries in risk levels. Some participants stated that they have been using a three-tier level similar to the Basel AML Index; others mentioned the use of four-tier level classifying countries into low, low-medium, medium-high and high risk.

⁷

See for a complete list of the 15 KFSIs: <http://www.financialsecrecyindex.com/methodology> (as of 18 July 2016).

Independent from the risk levels, it was stressed that the division between low and medium risk is less significant than division between medium and high risk because the high risk level typically determines when to carry out enhanced due diligence measures.

From a methodological point of view, the review group pointed out that it is arbitrary to determine a specific cut-off for the risk levels. There is also no known regulatory standard as to where the cut-off should be, thus institutions should apply their own categorisation for the risk levels and decide their classification for high risk countries based on their risk-appetite and institutional needs. Participants also expressed that the risk rating should be on a continuous scale and institutions could decide on a case-by-case in determining the high risk levels for certain countries.

The Basel Institute recommended consulting the sub-indicators of the Basel AML Index in combination with internal data when decisions are made to categorise countries as high risk.

6.5 Discussion on final ranking scores and plausibility check

The Basel Institute presented its preliminary results of the 2016 Public Basel AML Index to the review group. An excel sheet was distributed prior to the meetings which indicates the countries that have notably improved or deteriorated since last year. Most changes in the country risk ratings have been due to updated FATF Reports and/or changes in the FSI. The FSI added 13 countries to their ranking in 2015, which also impacted the rating of these countries in the Basel AML Index as an additional indicator was now available in the calculation of the overall score.

Overall, the review group did not identify any inconsistency or large outliers in the results, but discussed some of the ranking positions on the basis of the underlying methodology.

The participants noted for example Egypt being rated lower in risk to money laundering than countries such as France and Germany. The Basel Institute explained that these results were due to the use of FSI and US INCSR reports. Countries such as France and Germany are rated as higher risk within these indicators because of their relative large size of the economy and financial services offered abroad.

Feedback was also provided referring to Namibia and Lesotho, which are rated as high risk. Their risk ratings seem to be not updated due to their FATF-style regional bodies being underfunded and/or not consistent with their FATF follow-up reports. Moreover, their assessment cycle seems less frequent than others, leading to their AML/CFT framework still being assessed on the basis of outdated MERs. In order to address this issue the Basel Institute has already taken steps in the past by considering FATF follow-up reports indicating progress made based from an older MER. FATF follow-up reports are not available for every country, but without alternative sources, the Basel Institute is required to rely on the enforcement of a consistent application of the FATF assessment across all the FATF-style regional bodies.

Another issue that was raised by the review group is the fact that some countries are not being rated by the FSI or US INCSR and therefore their size of economy and the amount of financial services are not being taken into consideration in the risk assessment. The Basel Institute will also consider reviewing the use of the US INCSR indicator for countries not classified as a concern for money laundering in Basel AML calculations to better reflect the vulnerability of countries when it comes to the size of the economy and financial services.

7 Expert Edition

In addition to the publicly available Basel AML Index, the Basel Institute offers a subscription-based Expert Edition, which is a more comprehensive country risk assessment tool to assist financial institutions and other stakeholders to deal with diverse compliance and regulatory purposes. In contrast to the Public Edition, it provides:

- An overview of 203 countries according to their risk level in money laundering and terrorist financing;
- Per country details of all sub-indicators
- Online access to web-interface including the option to download the data as an Excel file;
- Monitoring of U.N. sanctions, U.S. State Sponsor of Terrorism lists and FATF Public Statements; and
- Periodic updates and email notifications/alerts.

Public version	Expert Edition
Overall score	Overall score, 14 sub-indicators and sanctions list
149 countries	203 countries
Update annually	Periodic Updates
For general public	For financial institutions, compliance & due diligence experts, AML/CFT regulators, Financial Intelligence Units (FIUs), academics & researchers
Provided as-is	Expert advice and tailor-made solutions are available upon request

Table 3: Public vs. Expert Edition

7.1 Why use the Expert Edition?

The rationale for creating the Expert Edition is to assist financial institutions and reporting entities that are facing considerable regulatory, legal and reputational risk. With a subscription to the Expert Edition, financial institutions and other reporting entities have a new standardised AML country risk-rating tool at their disposal to mitigate money laundering and terrorist financing risk. The Expert Edition can be used as a stand-alone solution to satisfy regulatory requirements or as an independent benchmarking tool to validate in-house risk assessments.

Our in-house experts on anti-money laundering and compliance have extensive experience and insight into industry practice and regulatory requirements regarding country risk models. In the development stages and during the Basel AML Index annual review, the Basel Institute further extensively consults with key stakeholders and representatives from academia, finance (e.g. Wolfsberg Group and its member banks), international organisations (e.g. UNODC), law enforcement and regulatory institutions.

The financial industry considers the Expert Edition an invaluable tool for regulators and financial institutions, and particularly values its foundation in scientific research and the independence of its

developers. Within the first year of its existence, the FATF listed the Basel AML Index in its publication as one of the **Indexes to be considered for country or geographic risk factors**.⁸

Since the launch of the Basel AML Index in 2012 more than 120 institutions have subscribed to the Expert Edition and consider it an indispensable tool for their risk assessment. Subscribers include not only financial institutions and firms, but also public institutions and financial regulatory authorities such as the:

- Bank of Canada
- Dubai Financial Service Authority
- Europol
- International Finance Corporation of the World Bank
- International Monetary Fund
- Reserve Bank of Australia
- Reserve Bank of New Zealand
- UK HM Treasury
- Various FIUs and Central Banks.

Since the Basel Institute is a non-profit organisation, access to the Expert Edition is provided free of charge to academics, public and supervisory institutions and other relevant non-profit organisations. Commercially oriented institutions are charged an annual subscription-based fee of 2000 CHF (or more depending on usage levels), which is used for non-commercial purposes and serves to fund the research, development and maintenance costs of the Basel AML Index.

For more information regarding the Expert Edition please see this link:

<https://index.baselgovernance.org/expert-edition-intro>

8 About the Basel Institute on Governance

The Basel Institute on Governance is an independent not-for-profit competence centre specialized in corruption prevention and public governance, corporate governance and compliance, Collective Action, anti-money laundering, criminal law enforcement and the recovery of stolen assets.

Based in Switzerland, the Basel Institute's multidisciplinary and international team works around the world with partners in the public and private sector to counter corruption and other financial crimes, and to improve the quality of governance globally.

⁸

FATF Report *Specific Risk Factors in the Laundering of Proceeds of Corruption - Assistance to reporting institutions*, FATF 2012: 31. <http://www.fatf-gafi.org/media/fatf/documents/reports/Specific%20Risk%20Factors%20in%20the%20Laundering%20of%20Proceeds%20of%20Corruption.pdf> (as of 18 July 2016).

The Basel Institute is affiliated with the University of Basel and regularly works with international organisations and other institutions, including the World Bank, United Nations Office for Drugs and Crime (UNODC), Organisation for Economic Cooperation and Development (OECD), Council of Europe, International Monetary Fund, the Egmont Group and Interpol.

9 Annex 1

Overview of risk indicators including weighting

This table provides you with our table of sources and weightings in compiling the Basel AML Index.

Risk Indicators	Weighting	Type	Link
ML/TF Risk	65%		
1.) FATF Member countries Mutual Evaluation Reports; Assessment of the 40+9 recommendations	30%	Expert Assessment (Mutual Evaluation Country Report)	http://www.fatf-gafi.org/
2.) Financial Secrecy Index (Tax Justice Network)	25%	Composite Index Score (qualitative + quantitative data)	http://www.financialsecrecyindex.com/
3.) US State Department International Narcotics Control Strategy Report (INCSR): Volume II Money Laundering and Financial Crimes	10%	Expert Assessment (List of jurisdictions according to their level of concern)	http://www.state.gov/j/inl/rls/nrcrpt/2016/index.htm
Corruption Risk	10%		
4.) TI Corruption Perceptions Index (CPI)	10%	Composite Index (Survey/perception based data)	http://www.transparency.org/cpi2015/
Financial Transparency & Standards	15%		
5.) Doing Business Ranking (World Bank) Business extent of disclosure index	1.875%	Expert Survey	http://data.worldbank.org/indicator/IC.BUS.DISC.XQ
6.) WEF Global Competitiveness Report (GCR) - Strength of auditing and reporting standards	5.625%	Expert Survey	http://reports.weforum.org/global-competitiveness-report-2015-2016/

7.) WEF GCR – Regulation of securities exchanges	5.625%	Expert Survey	http://reports.weforum.org/global-competitiveness-report-2015-2016/
8.) World Bank IDA Resource Allocation Index (IRAI) – Financial Sector regulations	1.875%	Expert Assessment	http://go.worldbank.org/S2THWI1X60
Public Transparency & Accountability	5%		
9.) International IDEA Political Finance (Political disclosure)	1.6667%	Public data assessment	http://www.idea.int/political-finance
10.) Open Budget Index – Budget transparency score	1.6667%	Expert Assessment	http://internationalbudget.org/what-we-do/open-budget-survey/
11.) World Bank IDA Resource Allocation Index (IRAI) – Transparency, Accountability and Corruption	1.6667%	Expert Assessment	http://go.worldbank.org/S2THWI1X60
Political & Legal Risk	5%		
12.) Freedom House – Freedom in the World (Political Rights and Civil Liberties) & Press Freedom Index	1.6667%	Expert Survey	https://freedomhouse.org/report/freedom-press/freedom-press-2015 & https://freedomhouse.org/report/freedom-world/freedom-world-2016
13.) WEF GCR – Institutional Pillar	1.6667%	Expert Survey	http://reports.weforum.org/global-competitiveness-report-2015-2016/
14.) WJP – Rule of Law	1.6667%	Expert and Public Survey	http://worldjusticeproject.org/rule-of-law-index