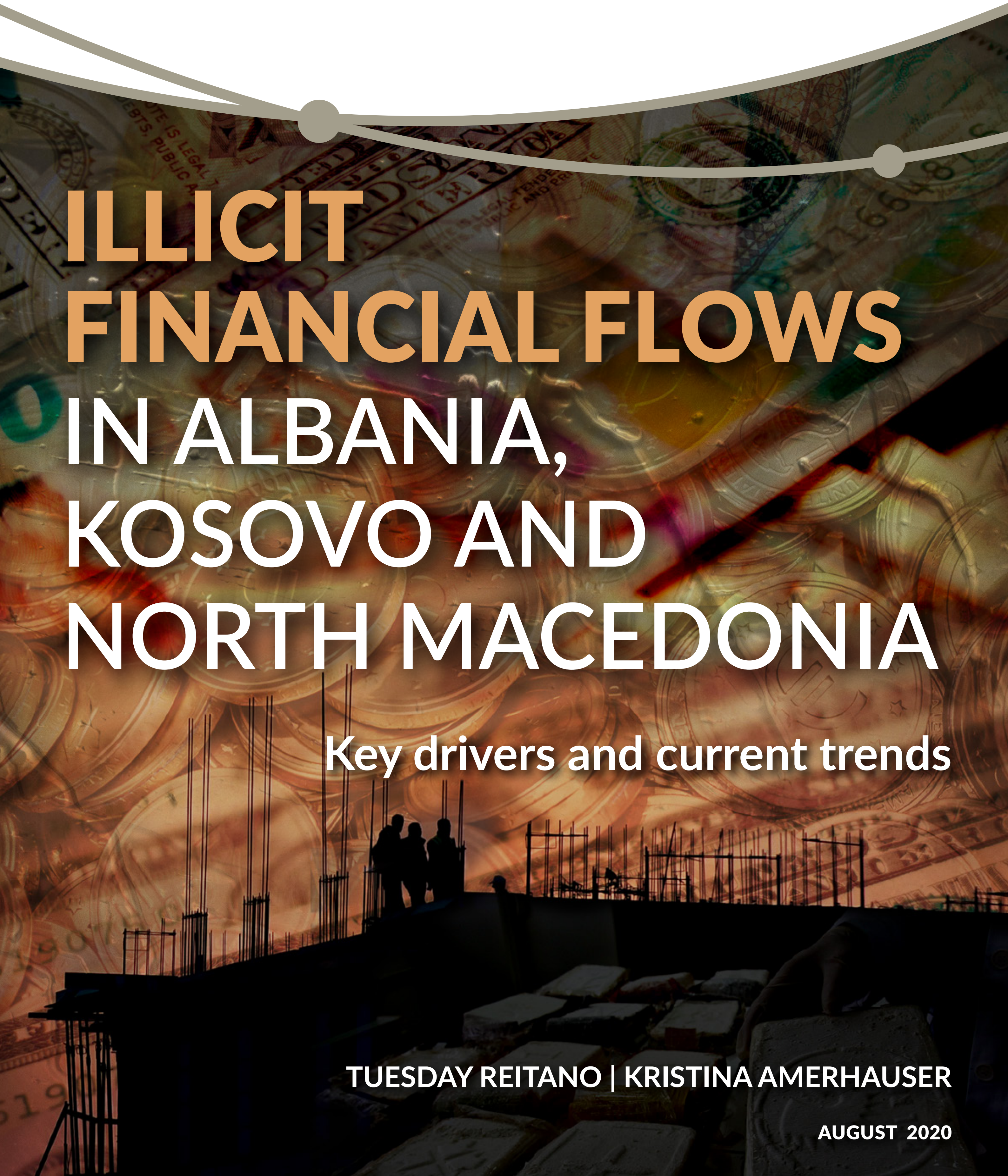
POLITICAL ECONOMY REPORT

GLOBAL INITIATIVE
AGAINST TRANSNATIONAL ORGANIZED CRIME



ILLICIT FINANCIAL FLOWS IN ALBANIA, KOSOVO AND NORTH MACEDONIA

Key drivers and current trends

TUESDAY REITANO | KRISTINA AMERHAUSER

AUGUST 2020

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Tuesday Reitano
Kristina Amerhauser

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This assessment of illicit financial flows is part of the Global Initiative's wider engagement in the Western Balkans and the Civil Society Observatory to Counter Organized Crime in South Eastern Europe (SEE-Obs). SEE-Obs is a platform that connects and empowers civil-society actors in Albania, Bosnia and Herzegovina, Kosovo, Montenegro, North Macedonia and Serbia. It aims to enable civil-society actors to identify, analyze and map criminal trends and the impact of these on illicit flows, governance, development, inter-ethnic relations, security and the rule of law, and supports them in their monitoring of national dynamics and wider regional and international organized-crime trends.

The report is based on data, information and analyses collected by civil-society actors. In particular, it draws on interviews with and input reports from nine experts in Albania, Kosovo and North Macedonia. We thank them for their valuable contributions and frank and constructive engagement throughout the process. Special thanks also to Walter Kemp, Fatjona Mejdini, Ugi Zvekic and Fabian Zhilla of the SEE-Obs team.

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ABOUT THE AUTHORS

Tuesday Reitano is Deputy Director at GI-TOC. Tuesday spent 12 years as a policy specialist in the United Nations system, including with the UN Development Programme (UNDP), the UN Development Group (UNDG) and the UN Office on Drugs and Crime (UNODC). She has authored several policy-orientated and academic reports with leading institutions, such as the UN, World Bank and OECD, on topics ranging from organized crime's evolution and impact in Africa to human smuggling, illicit financial flows, and the nexus between crime, terrorism, security and development. Tuesday is the lead author of an OECD flagship publication: Illicit Financial Flows: Criminal Economies in West Africa. Tuesday is based in Geneva, Switzerland, with her family.

Kristina Amerhauser joined GI-TOC in October 2018. She is currently an analyst conducting research on the Western Balkans and working with SEE-Obs. Kristina holds a master's degree in advanced international studies from the Vienna School of International Studies, a BSc in international business from the Vienna University of Business and Economics and a BA in development studies from the University of Vienna. She is based in Vienna.

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Cartography: Paulina Rosol-Barrass

Please direct inquiries to:
The Global Initiative Against Transnational Organized Crime
Avenue de France 23
Geneva, CH-1202
Switzerland

www.globalinitiative.net

CONTENTS

ACRONYMS AND ABBREVIATIONS

ALL	Albanian lek
AML	Anti-money laundering
AML/CFT	Anti-money laundering / countering the financing of terrorism
EU	European Union
EULEX	EU Rule of Law Mission in Kosovo
FATF	Financial Action Task Force
FIU	Financial Intelligence Unit
GDP	Gross domestic product
GFI	Global Financial Integrity
GI-TOC	Global Initiative Against Transnational Organized Crime
IFFs	Illicit Financial Flows
IMF	International Monetary Fund
KFOR	NATO Mission for Kosovo
ML/TF	Money laundering / terrorism financing
MONEYVAL	Council of Europe Committee of Experts on the Evaluation of Anti-Money Laundering Measures
NBRNM	National Bank of the Republic of North Macedonia
PPE	Personal protective equipment
SDG	Sustainable Development Goal
SEE-Obs	Civil Society Observatory to Counter Organized Crime in South Eastern Europe
STR	Suspicious transaction report
TJN	Tax Justice Network
UNMIK	United Nations Interim Administration Mission in Kosovo
UNODC	United Nations Office on Drugs and Crime
VAT	Value-added tax

© Peter Endig/Picture Alliance via Getty Images

EXECUTIVE SUMMARY

Illicit financial flows (IFFs) – defined by the UN as 'money that is illegally earned, transferred or used and that crosses borders' and that is generated from three sources: criminal activity, corruption and tax fraud[1] – are a significant challenge for the countries of the Western Balkans. This report considers the dynamics of IFFs in the region, with a focus on Albania, Kosovo and North Macedonia. It is intended to complement the numerous assessments done at the behest of multilateral organizations, and as part of the EU accession process, by drawing on a civil-society perspective of the phenomenon.

Following the model provided by UN Task Force on Financing for Development, the report examines the *components* of IFFs, which are the means by which they are generated, and the *channels* by which they are moved through national, regional and transnational regions. IFFs often end up commingled with or laundered into the legitimate economy, or held offshore in secrecy jurisdictions.

Because they are made up of criminal acts, it is almost impossible to research IFFs precisely. The findings of this report draw from interviews with knowledgeable national and regional interlocuters within government, civil society and the private sector, and from cases where evidence is revealed through seizures, indictments or prosecutions, as well as available documents. Considerable benefit was gained from GI-TOC's Civil Society Observatory to Counter Organized Crime in South Eastern Europe (SEE-Obs), which provided additional experience and anecdotal evidence of the ecosystem of crime that enables IFFs.

The research was conducted in two phases: an initial round of key informant interviews in November and December 2019, and a follow-up round of analysis in May 2020. More than 60 semi-structured interviews were conducted in total. A literature and media review was also conducted, in three languages, English, Albanian and Macedonian, which included national reports and data, international reports and assessments, including the EU accession reviews and MONEYVAL reports, and reporting from local, regional and international presses.

The field research revealed that the terminology of 'international financial flows' has little traction in the region. A number of the interlocutors did not understand it immediately, and all of the participants had different working definitions of the problem. This will have consequences for the ability to deliver programming to counter IFFs in an integrated and holistic way. However, the UNCTAD-UNODC task force on IFFs has suggested that the value of the IFF approach is more conceptual than practical: it offers a general vocabulary to understand and convey the interlocking nature of the criminal ecosystem, but technical responses need to be more specific to the different components and channels.[2]

The report makes seven key conclusions about IFFs in the region and concludes by recommending that the IFF debate be used to frame a more inclusive dialogue on the corruption and crime ecosystem, and to mobilize popular support for changing the culture of governance and resource allocation in the region.

Key conclusions

1. All evidence suggests that the scale of IFFs is large, and that they are enabled by a number of structural features of the countries in the region: their integration; their large informal economies, which represent 30–40% in all three countries; and the overall weakness of the state, state institutions and democratic cultures. Geographically, the region has long served as a gateway route between Asia and Europe for drugs, migrants and a host of trade goods. Despite the technical progress made towards compliance with anti-money-laundering and combating-financing-of-terrorism (AML/CFT) frameworks, and advancing anti-corruption and transparency measures, the systemic features undermine real progress and results.
2. There is a sharp contrast between the scale of opportunities in the criminal economy and the legitimate economy. In a region where the average monthly salary falls between €400 and €600 per month, and youth unemployment exceeds 20%, the transit trade in drug trafficking is estimated to be worth more than half a billion euros each year in Albania alone. Given the context described in the previous point, the illicit economy arguably offers greater livelihood opportunities than the licit economy.
3. IFFs are also enabled by chronic levels of corruption and graft that permeate every level of the state, ranging from transactional bribery to grand-mal corruption in public procurement. Kickbacks are considered a perk of office, and politically connected figures enjoy privileged access to lucrative industries and political protection for their interests. Given the widespread sense of impunity in

the state, ordinary citizens see little incentive to adhere to the rule of law. Recent assessments by international bodies suggest that governments in the region are actively taking steps to reduce oversight by independent institutions, erode checks and balances, and undercut efforts for transparency and accountability. This includes attacking the independent media and closing down space for civil society.

4. Party political financing is a particular point of vulnerability for the anti-IFF and broader development agendas, and there is little evidence of effective regulation. While there are nominal limits on private contributions, they are poorly monitored and easily circumvented. In addition to anecdotal reports of 'black briefcases' passed to political figures, various revelations have disclosed financial manipulation by organized crime and other domestic and foreign actors in the political life of all three countries. It may be assumed that political figures with secret backers will be less responsive to their electorate.
5. In all three countries, many transactions occur in cash. Even multi-million-euro cash payments for luxury apartments are considered normal. This reflects the informal nature of the economy, but is also a means by which individuals and corporations can avoid or reduce their tax burdens. This imposes significant limitations on AML/CFT measures and other regulations intended to ensure the integrity of the financial system. Because their provenance cannot be monitored, cash transactions remain outside of the sightline of the formal financial system. This is an enormous boon to those keen to launder criminal money, both domestically and transnationally. The scale of undeclared cross-border cash transfers is estimated to be large – recent seizures found individuals carrying more than €1 million in cash in private cars – but the prevention of cash-smuggling is reportedly a low priority for law enforcement and border control officials.
6. Money laundering is done in all manner of ways, particularly in the real-estate sector. It begins with the financing of new residential or commercial construction, continues with financing the construction contracts and undercounting the value of labour in construction, and again with the sale of the finished buildings. Collusion in these forms of illicit activity has been identified at all points in the chain, including contractors, real estate agents, notaries, lawyers and bankers.
7. Two of the three countries covered in this report have met the benchmarks required to continue towards EU accession. This is an important achievement. However, a closer examination – particularly of the rate of successful prosecutions – reveals the shortfall of these technical instruments. To make a real impact in addressing IFFs will require reducing informality, changing the normalization of corruption and clientelist politics, and breaking down protection networks at the top of the political system.

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INTRODUCTION

Understanding and estimating IFFs in Albania, Kosovo and North Macedonia is a challenging undertaking, as there is no universally accepted definition or a single indicator that can comprehensively capture the phenomenon. Being illicit, these flows are hard to track. However, every reliable indicator does suggest that the scale is significant and growing. In 2015, Global Financial Integrity (GFI) estimated that IFFs could equal some 5.9% of the region's GDP,[3] which proportionally far exceeds the estimates of global illicit outflows, pegged in the region of 3–5% of global GDP.[4]

IFFs include mechanisms that promote rent-seeking and criminal behaviour. They allow wealthy and exploitative elites and criminal actors to launder the profits of their ill-gotten gains, to evade taxes, use political power for personal gain, conceal the ownership of assets and pass on their wealth without contributing to the tax bases of their countries. They thereby undermine efforts to limit wealth inequality, reduce governments' capacities to support development and inclusive growth goals, and significantly undermine the rule of law.

It is for this reason that the Sustainable Development Goals (SDGs) recognize IFFs as a compelling threat to governance and justice globally. Target 16.4 pledges to, '[b]y 2030, significantly reduce illicit financial and arms flows, strengthen the recovery and return of stolen assets, and combat all forms of organized crime'.[5]

The fight against corruption and organized crime has been identified as an important precondition to EU accession, a long-standing geopolitical goal of the countries of the Western Balkans. In the EU's diagnosis, these countries show clear elements of state capture, including links with organized crime and corruption at all levels of government and administration, as well as a strong entanglement of public and private interests. All this feeds a sentiment of impunity and inequality. There is also extensive political interference in and control of the media. A visibly empowered

FIGURE 1 The Western Balkans 6 region

and independent judiciary and accountable governments and administrations are essential for bringing about the lasting societal change that is needed.[6]

The EU enlargement process paper also notes that 'the region's economies are uncompetitive, with too much undue political interference and an under-developed private sector'.[7] The process requires progress on the rule of law and competitiveness, including reduced levels of corruption and organized crime, as a precondition. The EU acquis prescribes a clear set of targets that each of the Western Balkan countries would need to reach before membership could be considered.[8]

Yet, despite considerable investment by the EU and other partners, even relatively cursory assessments suggest that the states of Albania, Kosovo and North Macedonia are far from likely to achieve the SDG target. Money circulates illicitly in and out of the Western Balkans in every direction, enabled by an ecosystem of crime, corruption and corporate evasion that permits IFFs on a staggering scale.

IFFs in the Western Balkans are manifold, multi-directional and proportionally massive as a percentage share of GDP. Yet the term is little used locally and the phenomenon understudied. This is partly because it is a new concept, which has been layered over long-standing efforts to strengthen the legal and regulatory AML/CTF and economic crime frameworks in the region.

Money circulates illicitly in and out of the Western Balkans, enabled by an ecosystem of crime, corruption and corporate evasion that permits IFFs on a staggering scale.

The benefit of the IFFs concept is that it encapsulates the entire ecosystem of criminal and corrupt behaviour that bleeds value from national economies. The concept is fundamentally developmental – it was created to highlight the harms of illicit flows on governance, socio-economic development, poverty and inequality.

What are IFFs?

IFFs have been defined and redefined, and still the definitions remain broad, vague and disputed, despite their inclusion in policy frameworks as universal as the SDGs. The term tends to serve as a conceptual umbrella over a wide range of transnational and domestic threats that describe activities within a spectrum of illicit international trade and finance.[9] The lack of an accepted formal definition is not just an academic concern. The conceptual confusion is a critical weakness in research and analysis, and in the creation of policy and programmes to respond to the problem.

It was notable, for example, how often the term IFFs had to be explained to the people interviewed for this report. Some interlocutors saw IFFs as synonymous with 'money laundering' or with 'organized crime', which created challenges within the interviews. Different understandings of the problem and its scope resulted in a lot of contradictory estimates of the proportional levels of IFFs in the region, with interlocutors tending to favour their own areas of expertise. For example, a customs official suggested that more than 95% of IFFs are generated from trade mis-invoicing, while a drug-control enforcement official claimed a similar percentage is generated by drug trafficking.

This report will adopt the UN definition of IFFs: 'money that is illegally earned, transferred or used and that crosses borders', and that is mainly generated from three sources: criminal activity, corruption and tax fraud.[10]

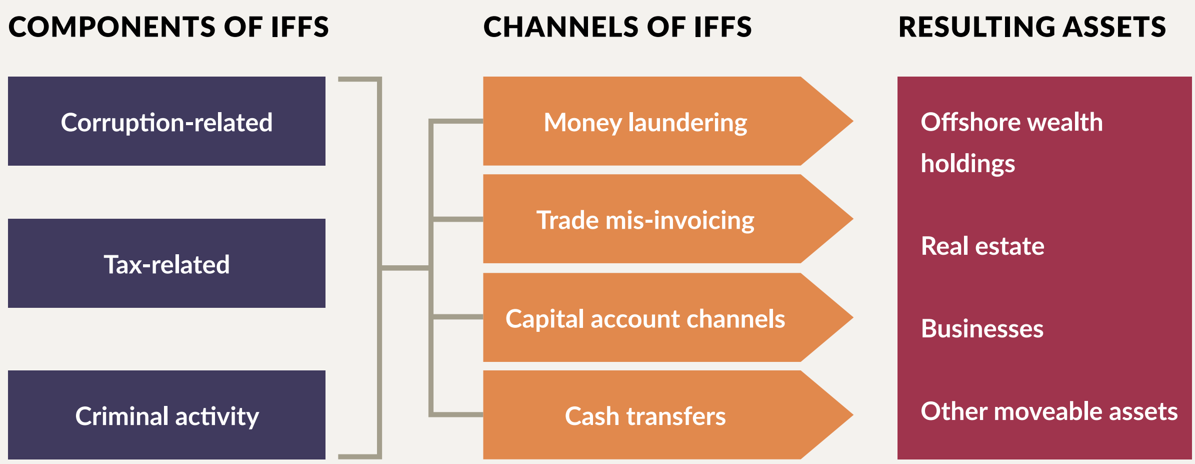

FIGURE 2 Components and channels of IFFs

SOURCE: Financing for development: Progress and prospects. Report of the Inter-agency Task Force on Financing for Development 2017, https://developmentfinance.un.org/illicit-financial-flows

Financial flows can thus become illicit in three ways: from the onset, when they are earned by a predicate crime; when legitimately earned money is moved or transferred through the financial system in ways that make them illicit and when they are used for purposes of corruption, or when they are finally laundered or diverted overseas.

This highlights the challenge of putting an accurate monetary value to IFFs. With multiple points in their value chain where they can be measured, there is always a risk of double counting. In this sense, both the customs official and the drug-control official might be correct. It is more than possible that illicit proceeds from drug trafficking could be used to corrupt local officials, then laundered overseas through trade mis-invoicing. For this reason, therefore, the concept of IFFs is primarily valuable as an analytical tool. By incorporating the ecosystem of organized crime, corruption, and corporate crime, it covers all the ways in which value is taken from a country's economy to the detriment of development.

To explore IFFs in the Western Balkans, this report will follow the two-part structure provided by the UN Task Force on Financing for Development (Figure 2). It will first examine the three criminal *components* of IFFs – corruption, organized crime, and tax-related activities – and then the four *channels* of IFFs: money laundering, trade mis-invoicing, cash transfers, and capital account channels.

Methodology

As the discussion above highlights, a comprehensive picture of IFFs cannot be captured by a single trade or financial indicator. A combination of quantitative indicators and qualitative assessments is required to fully interpret the complex nature of the phenomenon. Indeed, the UNCTAD-UNODC Task Force on IFFs concluded that, given the numerous components and channels comprising the IFF concept, it was better to keep the issue disaggregated and to look at it as an ecosystem of interrelated phenomena.[11]

The methodology for this report draws from a variety of sources. It is based on primary field research in the form of more than 60 semi-structured interviews conducted between December 2019 and May 2020 with bank officials, law-enforcement personnel, members of financial intelligence units (FIUs), prosecutors,

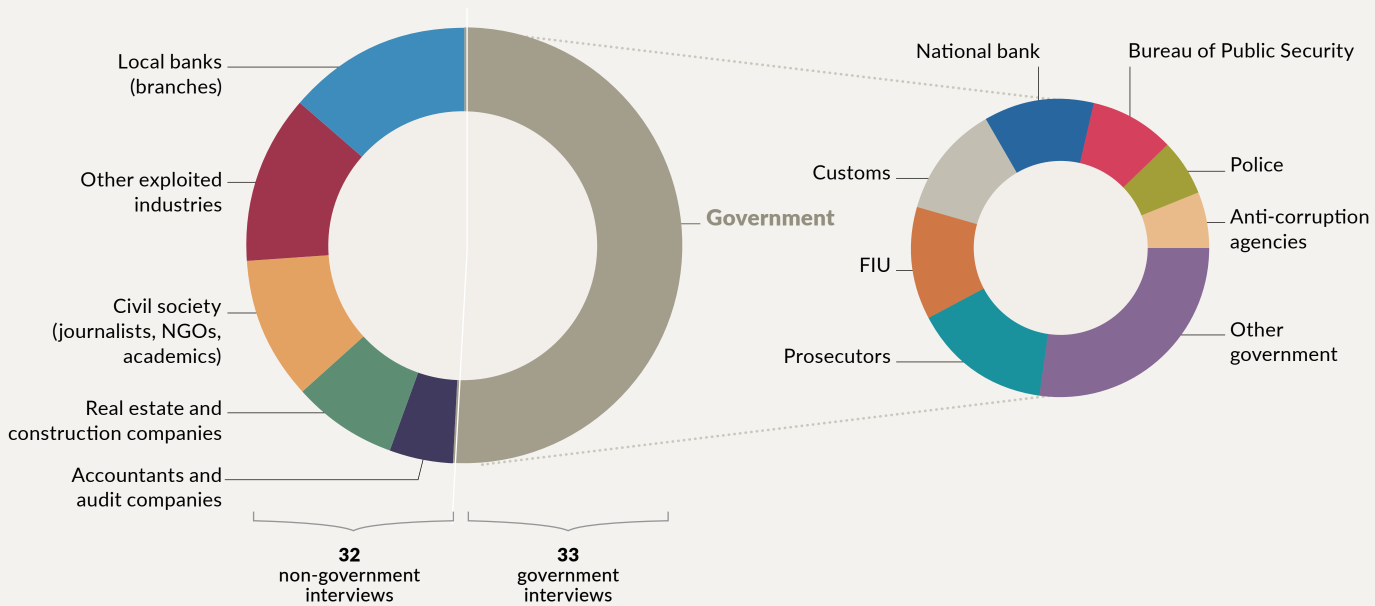

FIGURE 3 Overview of interview informants, n = 65

IFFs in the Western Balkans are manifold and proportionally massive as a percentage of GDP.

journalists and others. Figure 3 presents an overview of the composition of key informant interviews.

The field research was supplemented by a review of secondary literature, government evaluation reports and administrative guides and statistics. Freedom-of-information requests were sent to relevant authorities for additional information, with varying responses. Kosovo presented particular difficulties as there was less information available. Because of its unresolved political status, Kosovo is not always represented independently in regional studies conducted by the UN and other international agencies.

The core research team was made up of nine local researchers from Albania, Kosovo and North Macedonia with extensive experience in analysing organized crime, corruption, IFFs and money-laundering activities. A team of GI-TOC analysts screened all data to assess accuracy and reliability, and triangulated the qualitative and the quantitative data. The report was reviewed by internal GI-TOC regional and IFF experts, who also assisted in the development of recommendations.

Although IFFs are often assessed on their monetary value alone, it is important to keep in mind the discussion above. The numbers most likely reveal only a fraction of the problem, different components of IFFs are not comparable, and aggregation across the various channels could result in double-counting, all of which can interfere with effective analysis and policymaking to counter IFFs.[12]

The purpose of this report, therefore, is not to provide an overall estimate of the scale of IFFs in Albania, Kosovo and North Macedonia. Instead, it offers a political-economy analysis of key drivers and trends that enable IFFs in the region, and, in doing so, provides a richer understanding of the phenomenon and a framework upon which stronger responses can be designed.

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CONTEXTUALIZING IFFs IN THE WESTERN BALKANS

The goal of this section is to consider some of the key economic, criminal and governance features of the Western Balkans that make the region susceptible to IFFs. It finds that the structure of the economy, particularly the level of informality, facilitates illicit flows.

The interviews with expert interlocutors revealed features of the social, economic and governance profiles of the Western Balkans that have increased the region's vulnerability to IFFs. In particular, they highlighted how the interconnectedness of the three countries makes it particularly challenging to identify and implement national solutions. In a region that has shared a political ideology and its aftermath, as well as a protracted conflict that continues to drive insecurity and instability and leave lasting scars, IFFs are somewhat of a "wicked problem"[13] that are a deeply integrated part of this difficult reality.

The strategic geographic location of the Western Balkans is a key feature. Often described as the bridge between Asia and Western Europe, the area is part of the ancient and well-trodden Silk Road trade route for commodities and peoples. Significant infrastructure investments in recent years – much of it due to China's massive Belt and Road Initiative – has intensified the flows moving through the region, benefiting both legal and illegal commerce.

As is the case everywhere, the regional Western Balkan criminal economy thrives in the underbelly of the licit economy, and the increase in global trade and globalization has also helped organized crime to flourish in the Western Balkans. Migrants are smuggled and trafficked across the region on their way towards Europe.[14] Drugs, in particular Afghan heroin, move north-west along the Balkan route,

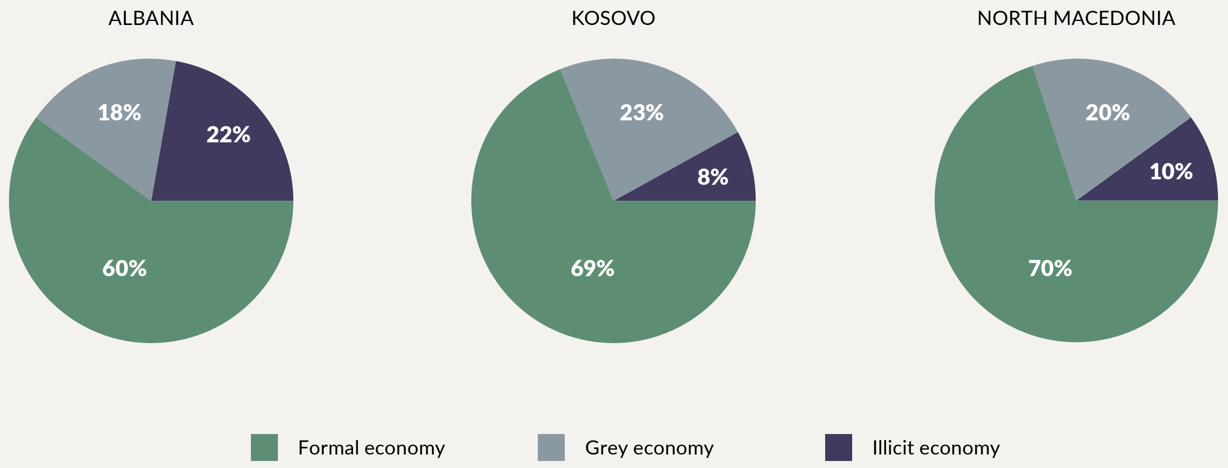

FIGURE 4 Estimates of formal vs informal sector economic activity in Albania, Kosovo and North Macedonia (% GDP)

SOURCE: Ernst and Young

while Latin American cocaine arrives in Albania and Montenegro by sea, and by plane in all countries of the Western Balkans. It is then smuggled westwards towards the EU and the UK, and eastwards towards Romania, Turkey and other countries.[15] Cannabis is produced and distributed widely,[16] and synthetic drugs cross the region (and are further processed there) on their way to Turkey and further east. There are numerous reports of arms trafficking and widespread counterfeiting and trade of illicit goods, including cigarettes, that are produced and smuggled across the region.[17]

As shown in Figure 4, a large portion of economic activity in the Western Balkans takes place in the informal economy, which the illicit economy also turns to its favour.

Informality designates economic activity that falls outside of the oversight of national financial and regulatory institutions. By definition, informal business transactions deal either in cash or through informal transfer mechanisms, such as hawala. In the Western Balkans, cash also underpins the largest portion of daily transactions in the legitimate economy.[18] This provides a wide-open playing field for the movement of illicit funds.

The extent of informal economic activity evolved from the post-war transition when cross-border smuggling was crucial to the process of state formation throughout former Yugoslavia.[19] Twenty years later, this legacy contributes to the interdependent nature of the Western Balkan economies, the fluidity of borders, and the firm entrenchment of rent-seeking practices in the informal and illicit economy by actors who are both (and sometimes simultaneously) criminally affiliated and state officials.

As also depicted in Figure 4, informality in Albania represents around 30–40% of the economy. Explicitly criminal transactions were estimated to be 22% of the GDP in 2017.[20] In Kosovo, the informal economy has been estimated at 31.7% of GDP, of which more than 8% appears likely to represent illegal forms of economic activity.[21] In North Macedonia, the informal economy is also estimated to be worth around a third of the country's GDP.[22] Although there has not been a formal estimate of the illicit economy, we can assume it will be of a similar proportion.

One of the primary reasons that illicit activity has become so prevalent in the Western Balkans is that the development of capacity and integrity in state institutions has not kept pace with the scale of trade.

National and international reports acknowledge the critical weakness of state institutions to regulate financial activity in economies that are dominated by small businesses with limited accounting systems and controls. In Albania, for example, 88% of businesses are registered as so-called 'small subjects', declaring less than €60 000 in income each year and having fewer than four employees. In Kosovo, more than 90%

of the businesses are micro and small enterprises.[23] With limited reporting and oversight obligations, these businesses can fly under the radar of national tax authorities.[24]

The low average wage rates in the region are also a factor. As shown in Figure 5, they average €400–600 per month, which implies that a great many people earn less than this. It is easy to understand why they might seek remunerative opportunities outside of the legitimate economy. High unemployment (in January 2020: 11.6% in Albania, 21.5% in North Macedonia, and 25.9% in Kosovo[25]) and low purchasing power drive many young people to search for other opportunities in both the informal and illicit economies.

All three countries have a dominant service sector. In 2018, trade in services accounted for 55.1% of GDP in North Macedonia[26] and 29.3% in Albania.[27] They also all have strong agricultural sectors: Albania's 18.4% of GDP in 2018 was the highest share of agriculture in the Western Balkans and in Europe.[28] The general industry sector, which includes construction, accounts for around 23.6% of North Macedonia's GDP, and 21.3% of Albania's.[29] Construction and real estate contributes 26.3% of GDP in Kosovo.[30]

INDICATORS	ALBANIA	KOSOVO	NORTH MACEDONIA
Population (million) (2018)[31]	2.87	1.85	2.8
GDP (US$ billion) (2018)[32]	15.10	7.94	12.67
GDP growth (2018)[33]	4.1%	3.8%	2.7%
GDP per capita (US$) (2018)[34]	5 268.8	4 302.3	6 083.7
Imports (% of GDP) (2018)[35]	45.40	55.60	72.90
Exports (% of GDP) (2018)[36]	31.70	26.40	60.30
Informal economy[37]	33% (2018)	30% (2016)	30–33% (2018)
Average monthly salary (€) (2019)[38]	400–450	475–525	550–670
Unemployment rate[39]	13.8% (2017)	29.4% (2018)	20.7% (2018)
Net migration (per 1 000 population)[40]	-7 (2017)	-8.90 (2016)	-0.50 (2017)
Corruption Perception Index ranking (2019)[41]	106/198	101/198	106/198

FIGURE 5 Key Western Balkans indicators at a glance

The regional economy relies heavily on remittances. Large financial inflows come from nationals residing in Western Europe and the United States, a significant portion of which arrives either in cash or through unsupervised non-bank financial services.

In 2018, the Bank of Albania reported that 1.15 million expatriate Albanians regularly send money back to their homeland, providing support to more than one-quarter of Albanian families. In 2017, Albanian remittances totalled €1.16 billion, of which 39% was sent in cash and 57% via non-bank financial services.[42] Total remittances sent to North Macedonia were estimated at €318 million in 2018, of which the majority similarly entered through informal channels.[43] Of the three countries, it is in Kosovo that remittances play the most crucial role as a source of income for citizens and businesses.[44] The Central Bank of Kosovo reports that €800 million flows into the country each year, while the Kosovar diaspora ministry estimates that remittances may total as much as €1.5 billion, which is equivalent to around 70% of state revenue.[45]

While remittances are an important and positive contribution to the region, their scale and informality provide an easy cover for moving illicit funds without detection. Because it is impossible to measure or to monitor the provenance of remittance funds, the potential for criminal money to join the flow is high. Global studies and best practices related to remittances strongly recommend that remittance transfers be shifted into the formal financial system.[46]

Albanians protest outside the government headquarters in Tirana, 2019. *© Armend Nimanl/AFP via Getty Images*

Governance features

Although the countries of the Western Balkans share many commonalities with the more mature democracies of Western Europe, and aspire to their standards, their democracies are still nascent and fragile. A mere two decades ago, the region was fraught with violent conflicts, and the ensuing practices of state capture, corruption, clientelism, and a lingering tendency towards authoritarianism impede efforts toward democracy.[47] Kosovo, which has made impressive progress, only began operating as an independent territory in 2008, giving it little time to build up post-war state institutions and a civic culture that could ensure an effective rule of law.

Electoral integrity is critical to the quality of democratic governance and the rule of law and to ensure that elected officials remain responsive to the needs of their citizens.[48] Non-violent, free-and-fair elections are also a critical requirement for EU accession for the Western Balkans countries. And while they have largely achieved multiparty elections free of violence,[49] there is a noted lack of transparency in political financing and legislative frameworks for party political financing are particularly weak. Such weaknesses can monetize politics through the covert funding of politicians by organized crime or other nefarious interests, resulting in a political system that is unconcerned with development and irresponsive to its electorate.[50] In the relatively new democracies of the Western Balkans, this is exacerbated by clientelism, with political parties that are based on personalities rather than ideology.[51]

The three countries covered by this report all have legislation that permits a combination of public and private financing for political parties and electoral campaigns.

However, public funding is limited, and political candidates get most of their funding from party membership dues and contributions from private individuals, companies and interest groups, both domestic and international. Albania restricts contributions to 1 million leke (€8 000) per candidate per electoral campaign; in Kosovo, political parties are restricted to €10 000 in donations per calendar year. All parties are required to report their funding sources within a period specified by law.

However, funding from anonymous private donors has been increasing across the region, the states have limited practical capacity to audit campaign financing,[52] and there have been repeated allegations of violations in all three countries under discussion. In Kosovo, a former employee of the EU Rule of Law Mission in Kosovo (EULEX) reported that political parties are hiding their finances and that the money they spend on elections far surpasses their declared income.[53] In 2018, the European Commission reported that independent audits of political-party finances found that the parties 'had significant amounts of unverifiable income and expenditures, persistent violation of financial accounting, international control and reporting standards, and showed instances of being in violation of the tax laws and the Law on the Prevention of Money Laundering'.[54] CSOs in Kosovo have been advocating for legal reform of political-party financing and strengthening the role of the Central Election Commission to monitor campaign expenses and costs. The current legislation enables the parliament to elect external auditors to examine the finances of political parties, which sets up possible conflicts of interest for politicians and favoured auditors. The government's response was to weaken the Bill on Financing Political Parties, a move which has come under considerable criticism.[55]

In June 2019, the German newspaper *Bild* set off a political scandal in Albania when it published leaked prosecution wiretaps that implicated senior party officials in vote-rigging in local elections in Dibra County in 2016 and the parliamentary election in 2017. The activities included collusion with criminal groups to buy votes, intimidation of teachers to vote for party candidates, and police interference with potential opposition voters.[56] Also in 2019, another recording was leaked that featured Mayor Vangjush Dako of Durres, Albania's second-largest city, in conversation with Astrit Avdylaj, a crime boss who was arrested for drug trafficking. It revealed the role that Avdylaj's gang had played in the electoral campaign, which included securing votes in the region of Shijak and Durres.[57]

Elections scheduled for April 2020 in North Macedonia were postponed due to the coronavirus pandemic. However, irregularities had already been observed, including political-party financing through unknown sources and clientelist links to the media. The opposition claimed that officials had also engaged in vote-buying and intimidation ahead of the 2011 and 2014 parliamentary elections and the 2013 local elections.[58] The Law on Financing of Political Parties, which was amended by decree in 2018, regulates funding to political parties. The notably independent Audit Office has reported on inconsistencies, but the control of the sources of funding falls to the Tax Authority, which is notoriously weak and susceptible to influence.[59]

Illegal foreign money also flows into domestic political campaigns in the region, doing the double service of both laundering the money and influencing the political agenda. An investigation by the Organized Crime and Corruption Reporting Project found evidence that an ally of Hungarian Prime Minister Viktor Orbán pushed over €3.2 million into North Macedonia through his media network. Ostensibly buying innocuous television advertisements for olive oil and fridge magnets – products that were not actually sold in North Macedonia – the huge payments aroused the suspicions of local financial police that Hungarian state money was being laundered into political activities favourable to Orbán himself.[60]

The past few years have seen a marked weakening of the oversight systems required to ensure the integrity of government processes and prevent corruption. Transparency International's 2019 Corruption Perception Index Report assesses all three countries as highly corrupt, and noted that their governments were taking active steps to diminish accountability measures.[61]

This includes steps to reduce the space for civil society and the media. Civil society – including independent journalism and the media, NGOs and CSOs, as well as academia – are relatively active in all three countries, attempting to hold their governments to account on their democratic, human rights and rule of law standards. Civic action, lead by activist oversight groups and often triggered by investigations by the independent media, have lobbied successfully for change in key legal frameworks, including on political transparency and accountability. However, a recent conference on civil society and organized crime in the Western Balkans, which included representation from the six states of the Western Balkans, observed that the media is captured by political interests, both domestic and foreign. Most TV and radio stations are state-owned and under the sway of politicians and their allies. At the same time, independent journalists and media houses struggle for funding and work under constant pressure. They are subject to levels of abuse, cyber-attacks and legal harassment that lead them to censor themselves to stay in business.[62] Politicians in all three countries have been known to actively denigrate journalists and interfere with independent reporting. Government and opposition parties make widespread use of disinformation and propaganda. In the 2019 Press Freedom Index, Reporters Without Borders ranks all three countries in the category of 'problematic media freedom'. In Albania in particular, the report noted that proposed anti-defamation legislation would curtail online media and make journalists more vulnerable to government pressure.[63]

Overall, the debate about IFFs and the potential for curtailing them is situated in a context of systemic weaknesses in governance that both enable illicit behaviour and actors, and impede the implementation of programmes to disrupt them.

KEY POINT SUMMARY

- IFFs are enabled by a number of features of the Western Balkans:
  - the geographic location as a corridor for both licit and illicit commerce;
  - the socio-demographic profile of a youthful population with high-unemployment;
  - sizeable informal economies that allow illicit flows to go unregulated.
- These are exacerbated by the governance weaknesses, including:
  - high levels of corruption;
  - democratic processes compromised by weak party-political identities and poor oversight of political financing;
  - increasingly restricted space for the voices of and oversight from independent media and civil society.
- Evidence suggests that governments are taking steps to progressively reduce, rather than strengthen, oversight, transparency, and checks and balances.

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COMPONENTS OF IFFs

This section of the report briefly considers how IFFs are generated through predicate crimes, such as corruption and organized-crime activities. Widespread corruption is seen as one of the greatest challenges to democratic development faced by the three countries. Specifically, the section examines the potential scale of illicit money generated by three forms of organized crime: drug trafficking, the smuggling of migrants and illicit trade.

As observed above, not all illicit financial flows have their provenance in crime. Legitimately earned money can also become illicit as it moves through the international financial system. However, a significant portion of IFFs run on the illicit proceeds of corruption, organized crime and tax-related crime. The Council of Europe's anti-money laundering MONEYVAL evaluations also indicate the scale and impact of IFFs from various predicate crimes in the Western Balkans which give rise to illicit finance.

Corruption-related crime

As the 2019 Corruption Perception Index Report saliently observes, 'across the region, countries experience limited separation of powers, abuse of state resources for electoral purposes, opaque political party financing and conflicts of interest'.[64] The scores of Albania, Kosovo and North Macedonia all declined since the previous year's Index, with Albania hitting a five-year low. As elites warp political, economic and regulatory systems to amass considerable wealth and maintain it for their own benefit, corruption creates a criminal ecosystem. The rule of law does not function without the support of the rulers.[65]

For citizens of these three countries, nepotism, clientelism and graft are embedded in the structure of their every interaction with the state, to the point that corruption has been described as part of the culture. People's trust in the rule of law and state institutions is very low, and the widespread perception of corruption and impunity creates few barriers for citizens themselves to engage in illicit enterprise. High unemployment (in January 2020: 11.6% in Albania, 21.5% in North Macedonia, and 25.9% in Kosovo[66]) and low purchasing power drive many young people to search for other opportunities in both the informal and illicit economies.

Corruption is a key component of illicit flows in its own right. Across the Western Balkans, criminal and other unscrupulous enterprises establish links with well-placed politicians, officials, and members of the judiciary and other state institutions to secure their various ends. By means of bribery, influence-peddling, brokering, abuse of power, and blackmail, they gain access to confidential information about ongoing judicial or law-enforcement plans and investigations. They may secure permits, concessions and public procurement contracts or ensure that their cross-border transport of goods is uninterrupted and uncontrolled. The rule of law is further curtailed through other obstructions of justice, such as witness tampering.

Although corruption is a worldwide problem, it is particularly damaging in developing countries and countries in transition. Unfettered corruption undermines the legitimacy and effectiveness of state institutions, compromises efforts to support sustainable development, deepens income inequality and deters productive investment. The funds generated from corruption may seem small in comparison to the profits of crime – drug trafficking, for example – but the harm caused by corruption is far-reaching and incapacitating.[67]

In North Macedonia and Kosovo, corruption is a principal source of money-laundering funds and a main threat to efforts to combat it.[68] In Albania, it is the second-largest source of IFFs after narcotics trafficking.[69]

It is difficult to calculate the extent of IFFs derived from corruption, but one indicator is the percentage of companies that report having paid bribes to do business with the state. The World Bank Enterprise Survey 2019 shows that 36.1% of companies in Albania received at least one bribe request in 2019, while those in North Macedonia reported 13%, as did 6% in Kosovo.[70] A similar study conducted by the United Nations Office on Drugs and Crime (UNODC) in 2012 finds far higher contact rates and prevalence of bribery.

Indicator	Country			
	Albania	Kosovo	North Macedonia	Regional average
Contact rate	85.10%	91.20%	78.18%	71.30%
Prevalence of bribery	15.70%	3.20%	6.0%	10.20%
Average number of bribes paid	4.60	7.70	6.70	7.10
Percentage of bribes paid in cash	50%	59%	17%	36%
Mean bribe (€-PPP)	904	1 787	689	881
Median bribe (€-PPP)	338	1 059	317	317
Prevalence of business-to-business bribery	24.10%	32.90%	25.40%	27.70%

FIGURE 6 Main indicators by country/area, Western Balkan region, 2012

SOURCE: UNODC, Business, corruption and crime in the western Balkans: The impact of bribery and other crime on private enterprise, 2013

NOTE: The regional average includes data from Albania, Bosnia and Herzegovina, Croatia, Kosovo, Montenegro, North Macedonia and Serbia. Contact rate: Percentage of businesses that had at least one direct contact with a public official or civil servant in the 12 months prior to the survey; Sources for additional indicators: local currency exchange rates and €-PPP conversion rates from Eurostat, WIIW and National Statistical Offices. €-PPP for Kosovo estimated on the basis of WIIW estimates.

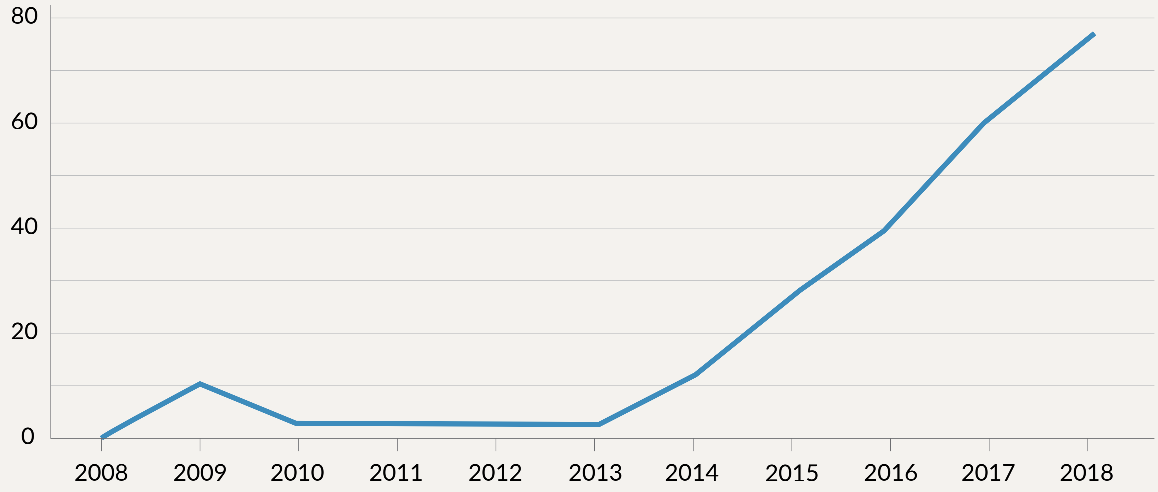

FIGURE 7 National procurement contracts issued as classified, Albania, 2008–2018

SOURCE: Gjergj Erebara, *Qeveria kontraktoi miliona euro shpenzime me kontrata sekrete*, BIRN, 27 May 2019, https://www.reporter.al/qeveria-kontraktoi-miliona-euro-shpenzime-me-kontrata-sekrete/.

Based on national reporting from across the three Western Balkans countries, the material cost of corruption can be estimated in the region of €80 million per year.[71] However, this is almost certainly a massive underestimation. Statistics that break down individual sources of corruption and graft, as we discuss below, suggest that a more appropriate estimate would be in the range of hundreds of millions of euros.

Public procurement contracts are a prime source of corrupt earnings. According to the OECD, 57% of foreign bribes are paid for to secure public procurement contracts, and 20–30% of the value of procurement contracts is lost to corruption.[72]

Figure 7 shows the sharp increase in contracts that were 'classified' – that is, not open for public tender – in Albania between 2014 and 2018. According to several sources in Albania, and consistent with the OECD estimate, up to 30% of the bid value of procurement contracts is paid in bribes.[73] In 2018/19, the government issued €679 million worth of public contracts, which would indicate bribery in the region of €200 million.[74] But it could be even higher. An investigation by one of Albania's biggest private television channels suggested that €300 million is lost annually to abuses in public procurement procedures, which would be nearly 45% of the 2018/19 contracts.[75]

Public procurement plays a similar role in corruption-related IFFs in Kosovo. Contracts worth €1.03 billion are budgeted for 2020, of which €672 million is for capital investment and €357 million for procurement of public goods and services.[76] Applying the OECD estimate, this could generate €205–308 million in bribes.

For the past ten years, Kosovo's government has allocated extensive funds to the construction of local roads and highways.[77] Such projects are extremely susceptible to corruption, as price-fixing, fraud in implementation, and the falsification of documents are all easy to implement and hard to detect.[78] In December 2018, for example, a 'ghost company' in Albania was discovered to have won an €18 million road-construction contract on the basis of false documentation.[79] In Kosovo, numerous reports have pointed to tender violations in the Gjilan highway project and road-construction segments from Gjakova to Shkodër and Prizren to Tetovo.[80]

Similarly, North Macedonia's Skopje 2014 project has raised serious concerns about public-procurement procedures. What began as an €80 million project to revamp the Macedonian capital with new facades, monuments and buildings has now devoured more than €680 million in state funds.[81]

However, a North Macedonian financial analyst said in an interview that government statistics suggest 'the number of crimes of abuse of power and authority is steadily increasing year by year, but the material damage is decreasing'.[82] He and other interlocutors also agreed that anti-corruption efforts have constrained corruption, particularly at the apex of politics and state institutions, but that it remains prevalent at lower levels. For example, the former head of North Macedonia's Special Prosecutions office was recently found guilty of abuse of office and sentenced to seven years in jail.[83]

Evidence across the region suggests that the criminal proceeds of corruption are laundered in much the same manner as proceeds from organized crime: through investments in businesses and real estate domestically, within the region, and overseas. As the Panama Papers revealed, corrupt politicians and officials also take advantage of tax havens to hide their wealth.

Organized crime

Profit-generating crime, and organized crime in particular, displaces productive economic activity, distorts competition, and discourages investment and entrepreneurship. Organized crime also tends to go hand-in-hand with corruption and wider governance failures as criminal groups actively undermine law enforcement, the justice sector, and political structures to suit their own ends. In addition, their use of violence as a means of market-regulation and profit-taking creates far-reaching social ills.

Organized crime in the Westerns Balkans is extensive, with a long history in the networks of Asia and Europe. There are increasing reports of the importance of Balkan criminal groups in the region and beyond.[84] Groups from Albania, Kosovo and North Macedonia are described as 'poly-criminal': involved in various criminal activities and able to adapt quickly to changing circumstances and markets. Their activities include drug trafficking (cocaine, heroin and cannabis) and the smuggling of humans and goods, including food and beverages, branded goods, clothing, footwear and tobacco.[85]

GI-TOC's Balkans Organized Crime Index was piloted for the six countries of the Western Balkans in 2018. Drawing from a range of regional and international experts, it assessed and ranked the forms of organized crime in the region, finding that drug trafficking, illicit trade and human smuggling were the three most prevalent and harmful illicit markets (Figure 8).[86] Our report, therefore, focusses on these three. However, the financial flows produced from lower-ranked types of crime still have significantly detrimental effects and, though poorly documented, they should not be discounted.

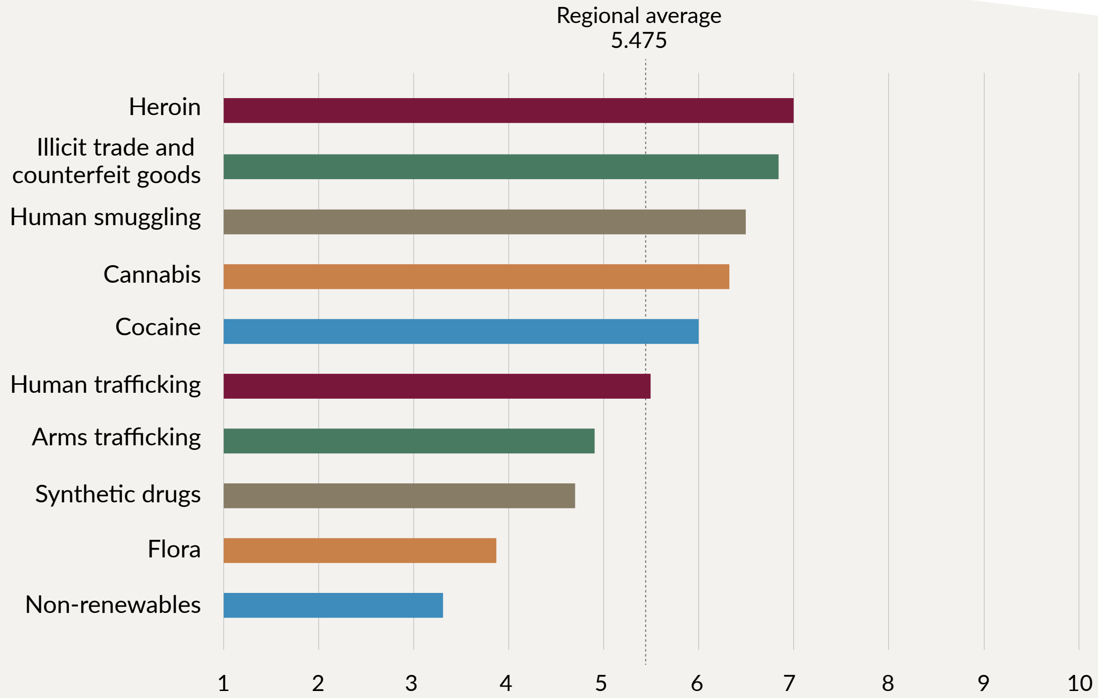

FIGURE 8 Ranking the scope and impact of illicit markets in the Western Balkans

SOURCE: GI-TOC Balkans Organized Crime Index[87]

Money and people flow freely between Albania, Kosovo and North Macedonia. People cross borders regularly for work and pleasure. No visas are needed, distances are short, and there are long-standing historical connections, especially among ethnic Albanians living in all three countries. This permeability also permits the movement of illicit goods, and the smuggling of people, cash and other assets.

Criminal groups cooperate with each other: migrant-smuggling networks arrange trips from North Macedonia to Kosovo and beyond; heroin-trafficking routes cross national borders, and contraband smuggling across the region (e.g. illicit tobacco and other products) is common.

Drug trafficking

The Balkan route is one of the most established drug-trafficking routes in the world, especially for heroin but also for cocaine and cannabis. In 2014, the UNODC estimated its market value at more than US$20 billion per year.[88] It links Afghanistan, the world's largest heroin-producing country, to the markets of Russia and Western Europe, west through Albania towards Italy, and north towards Austria. Cannabis cultivated in Albania is smuggled across the border to Kosovo, for domestic use or carried onwards to the European Union, and to North Macedonia, primarily for the Turkish, Bulgarian and Romanian markets. Cocaine moves from Albania and Kosovo to North Macedonia for domestic drug markets. Synthetic drugs produced in North Macedonia travel eastwards.[89]

Drug trafficking is the most important profit-maker for criminal groups in Albania. According to one expert interviewed, 70–90% of IFFs in Albania are generated through drug trafficking. The MONEYVAL assessment estimates that drug trafficking is the main source of laundered money in Albania, accounting for 42% of all money-laundering cases.[90]

While the Albanian government has tried to significantly reduce the cultivation of cannabis in the past years, its proceeds – along with heroin and cocaine – continue to be an important source of illicit financial flows.[91] The cannabis industry in the country has generated illicit profits for a large part of society, ranging from villagers who cultivate the crops to organized criminal groups who smuggle it abroad and sell it across the EU. During the peak cultivation period 2016–2017, it is estimated that the cannabis economy generated €2.2 billion.[92]

Proceeds from cannabis production provided the capital for Albanian and North Macedonian criminal groups to get involved in cocaine trafficking. Establishing direct contacts in Latin America, they transport the drug to the main European ports and distribute it across Western Europe.[93] The European Monitoring Centre on Drugs and Drug Addiction reports that Albanian organized-crime groups are increasingly present across European drug markets, and have moved up the cocaine-trafficking hierarchy from being foot soldiers and low-level distributors to now actively organizing shipments, thereby achieving a greater margin and undivided profits.[94]

Country	Drug group	Drug	Year				
			2012	2013	2014	2015	2016
Albania	Cannabis	Oil	1		11	6	
		Plants	3 300		55 141		253 629
		Resin	5		24	60	23
		Herb	21 138	20 673	101 726	11 353	30 015
	Cocaine	Salts	4	16	10	27	7
	Opioids	Heroin	88	47	73	37	57
Kosovo	Cannabis	Plants	1 058	151	693	256	No data
		Resin	1		24	60	No data
		Herb	1 238	85	738	462	No data
	Cocaine	Salts	7	4	21	1	No data
	Opioids	Heroin	94	23	10	10	No data

FIGURE 9 Annual drug seizures in Albania and Kosovo, 2012–2016 (kg equivalents)

SOURCE: UNODC Drug Seizure database, search for five most recent years in the database. All reported drug groups, minus non-INCB controlled substances, by country, https://dataunodc.un.org/drugs/seizures

Although data is unavailable for North Macedonia, the UNODC's database of drug seizures (as supplied by member states) highlights the large quantities of cannabis moving through the region (Figure 9). More recent data suggests that the amount of drugs passing through the region has escalated significantly in the last five years. In February 2018, for example, a single shipment of 613 kilograms of cocaine, worth €180 million, was seized in the Albanian port of Durres.[95] In the same year, the total seizure of cannabis was 20 365 tons.[96] With experts in Albania estimating that approximately 20% of all drugs passing through the country are seized,[97] the total scale of trafficking in narcotics could be considerable.

The margins achieved from cocaine-trafficking are reported to exceed €20 000 per kilogram, which creates enormous resources for reinvestment and corruption.[98] Proceeds from cocaine trafficking are also understood to fund and underpin other criminal activities, such as illegal firearms smuggling, money-laundering networks and facilities, the smuggling of other drugs and the illicit movement of people. The huge profits generated from drug trafficking are laundered in all manner of ways, both in the Western Balkans and beyond.

Legalization of cannabis cultivation in North Macedonia

In May 2016, North Macedonia adopted the Law on the Control of Narcotic Drugs and Psychotropic Substances, which allows for the production of cannabis and cannabis products for medical use, and the export of medicinal cannabis extractions.[99]

Between 2016 and 2018, 28 licences for cannabis cultivation and two extraction licences were issued.[100] In 2019, the government granted 31 new licences for cultivation, with 20 applications pending approval, and two licenses for cannabis extraction.

These concessions have been granted to individuals and legal entities from North Macedonia and abroad with notable connections to the current ruling political party, as well as former 'politically exposed persons' who have held prominent public positions and therefore are at risk for involvement in corruption.[101] The opposition party has accused the prime minister of steering cannabis licenses to relatives and allies.[102]

While the law was welcomed as a means to tax the cannabis trade, the sale of cultivation concessions has also been flagged as a means to create revenue for the political penholders, as the licencees will invest millions of euros. A long-awaited amendment to the legislation to allow the export of cannabis for recreational use is creating investment hype for a potentially explosive new market. The EU market for recreational marijuana has been estimated to be worth as much as US$39 billion a year.[103] The potential for IFFs is massive in a sector with extremely limited government capacity for regulation.

Moreover, a financial expert reported that most of the cannabis cultivated for medical use is not exported legally but instead is sold illegally into domestic and foreign markets, thereby generating another flow of illicit revenue.[104]

Illicit trade and counterfeit goods

The wars in Yugoslavia in the 1990s and the creation of seven new states, each with its sovereign borders, has also produced a vibrant criminal market in cross-border smuggling of normally legal goods. Sanctions, progressive privatization, differing tax rates and uneven supply created incentives for criminal groups to smuggle arms, food, oil, medicine, cigarettes and livestock.[105] Hubs that were created decades ago have endured to the present day. For example, Kukës and Tropojë in northern Albania were key trafficking centres and sources of supply for the Kosovo Liberation Army in 1999 as the border areas were largely unguarded by the Albanian and Serbian states.[106]

Today, illicit trade, particularly of tobacco products, continues to be a widespread and prominent criminal activity in the region. Most reports point to the importance of Montenegro[107] and Bulgaria in the tobacco trade, but it also plays a key role in Albania, North Macedonia, and particularly in Kosovo. The Zagreb Institute of Economics estimates that almost €18 million is derived from tobacco smuggling in Kosovo, and almost €20.5 million in North Macedonia.[108]

The illicit tobacco trade is facilitated in particular by differences in excise taxes between countries. In North Macedonia – the cheapest market for cigarettes in the region – a pack of cigarettes can be purchased for €1.50. Smuggled across the borders, it can be resold for as much as €5 or €7 in Germany.[109]

Illicit cigarettes and tobacco enter the region through major ports (such as Durres in Albania[110] and Bar in Montenegro[111]) and across land borders with Greece and Bulgaria. Smuggling often makes use of 'alternative border crossings' where the terrain is rough and mountainous, offering a relatively uncontrolled and safe passage. Mules transport the goods on the other side or local villagers are paid a small fee for their services. Illicit tobacco also travels southwards through Kosovo to Albania and North Macedonia on its way to Italy, Bulgaria, the Middle East and northern Africa.[112]

Illicit trade in tobacco products is a widespread criminal activity in the region.

The smuggling of migrants is one of the main sources of criminal revenue in the region.

The illicit tobacco trade and, to a lesser extent, the smuggling of counterfeit goods, have a significant impact in Kosovo, especially in the north of the country. Kosovar institutions are formally present in North Kosovo, but a parallel structure, financed by Serbia and paired with the accumulated power and wealth of certain influential businesspeople, has transformed this area into a grey zone of informality.[113] Serbian and Kosovar organized crime groups are reportedly cooperating to perpetuate the unregulated economy for their own ends, thus holding back the formalization of economic activity for the greater good of the countries' citizens.

Similarly, counterfeit goods produced in China and Turkey are widely available in the Western Balkans. Counterfeit sports shoes, cosmetics, accessories for mobile phones and other items transit through the region and find a local market. The EU identifies Albania as a transit point of particular significance for redistributing counterfeit products into European markets.[114]

Smuggling operations between Kosovo and Serbia seem to have increased in scale since customs tariffs were introduced on goods from Serbia and Bosnia and Herzegovina in late 2018.[115] The Kosovar government announced a reduction in barriers in early 2020, but whether smuggling activities will consequently decrease again will require close observation.[116]

Human smuggling

North Macedonia is located on a popular migrancy route from Turkey to Western Europe. Since the EU migrant crisis in 2015, it has been used by more than 1.5 million migrants.[117] The smuggling of migrants, organized mostly by Pakistani, Afghan and Macedonian nationals, is one of the most important sources of criminal revenue in the region. People pay smugglers between €2 000 and €3 500 to be taken from Greek refugee camps, such as Idomeni or Thessaloniki, along the Balkan route into Western Europe.[118] The Western Balkans leg alone costs between €800 and €1 000 on average. Migrants have to make additional payments along the route for lodging, food, services and additional bribes.[119] Although the Balkan route is currently officially closed, locals who live along the north–south corridor, from the Bogodorica border crossing with Greece to the Tabanovce border crossing into Serbia, facilitate migrants' transport and passage in exchange for cash, which then flows into the legitimate financial system. [120]

In 2018, a North Macedonian organized-crime group was identified as part of an international network that included groups from Albania, Bulgaria, Spain, the Dominican Republic, Honduras and Mexico. This network smuggled people from northern Albania and North Macedonia to the United States for the price of US$20 000–25 000 per person. In this single transfer, the network expected to earn around US$1 million.[121]

Kosovo received more than 900 migrants in the first two months of 2020 alone, 300 of whom were from Syria.[122] Most enter the country from Albania on their way towards Serbia. Some also re-enter from Serbia if they are unable to cross into Hungary.[123] One migrant told Radio Free Europe he had returned to Pristina from Serbia and was on his way to Albania to attempt to cross over from Durres into Italy and then to Germany. Some migrants had paid taxi drivers around €100 per person to take them illegally from the border with Albania to their destination. Others paid €200 to cross from Albania into Kosovo over a mountain road.[124]

The criminal proceeds of migrant smuggling end up in the legal financial system through various ways, including the purchase of luxury items and movable and immovable property, and investments in business ventures.

Migrants near Idomeni, at the border between North Macedonia and Greece, July 2020. *© Sakis Mitrolidis/AFP via Getty Images*

Tax-related crime

The third important component of IFFs is tax evasion. Tax evasion is distinct from tax avoidance, which is the minimization of taxes in accordance with the law. Tax evasion involved the illegal non-payment of taxes through failing to report income, reporting costs that are not legally allowed, or simply not paying taxes.[125] Corporations, as well as individuals, evade taxes, with significant differences in scale and impact.

Assessments of global losses due to tax evasion vary widely, but all are very large. The US Senate, for example, set revenue losses from tax evasion by US-based firms and individuals at around US$100 billion per year.[126] A World Bank study on Africa estimates tax evasion consistently within a range of 8–12% of GDP.[127]

Tax evasion is harmful for four interlinked reasons. It deprives states of tax revenue, constraining their ability to support national socio-economic objectives. It erodes the credibility of state institutions and undermines the rule of law. It exacerbates wealth inequality by allowing the wealthiest to hide their resources at the cost of the poor. Finally, it provides perverse incentives to public officials, financial institutions and corporations to increase their profits by circumventing regulations.[128]

Due to the size of informal economies in the Western Balkans, the level of tax revenue is significantly lower than elsewhere in Europe. The 28 EU members collect on average 40.3% of their GDP from domestic taxation in 2018.[129] North Macedonia's, Kosovo's and Albania's tax revenue stood at 17.65% (2018), 26.11% (2019) and 18.55% (2018) respectively,[130] and the majority of that comes from

Groups from Albania, Kosovo and North Macedonia are described as 'poly-criminal'.

value-added taxes (VAT) rather than income tax.[131] It is impossible to estimate exactly, but some of this disparity can also be attributed to evasive tax practices by corporate entities in the Western Balkans, facilitated by generally high levels of corruption and bribery, and weak state controls. A 2015 World Bank report estimates that 34% of VAT was not collected in Kosovo in 2012,[132] and a national strategy report indicates that Kosovo loses €8 million each year in the construction sector through the non-payment of taxes, and €11 million in the trade sector.[133]

Legal actions against companies for tax evasion provide an insight into the scale and strategies employed. Investigations by Kosovar institutions found businesses using shell companies – registered companies that make financial transactions but do not conduct any tangible business – and fictitious transactions to escape paying taxes.[134] Another common strategy is to issue goods without invoices to circumvent VAT. In the period 2006–2016, non-issuance of fiscal receipts was the leading detected form of tax irregularity in North Macedonia.[135]

Labour-intensive industries like construction or tourism evade taxes by under-declaring the number of workers on their payroll, declaring lower wages, or paying wages in cash.[136] Paying cash wages may seem like an informal-economy practice, but corporations with large payrolls in the construction or hotel industries systematically do so to avoid paying taxes and employee social-security contributions. This practice is perhaps culturally tolerated, but it should not be, as it contributes to the sizeable informal economy, which in turn reduces the tax base, increases worker vulnerability, and enables a facilitating environment for other forms of illicit or illegal activity.

To enforce and increase fiscal discipline, North Macedonia's Public Revenue Office publishes a blacklist of tax debtors every three months based on VAT, income tax, personal income tax, compulsory social-security contributions, excise taxes, and customs duties. In 2019, the net debt was over 10 billion denars (about €163 million).[137]

In September 2019, the Albanian prosecution office published a list of companies that were under investigation for tax evasion because of false VAT invoices.[138] On the list were several well-known concessionary and construction companies utilizing similar strategies to those discovered in Kosovo to reduce their tax burden. Yet only low-income individuals have so far been identified: those who allowed their names to appear as the owners of such ghost companies in exchange for a small payment.[139]

Evidence from all three of the Western Balkan countries suggests that most of these profits are transferred out of the region to tax havens and secrecy jurisdictions with very low tax rates, where the funds and account-holders become untraceable.[140] The money channelled out of the Republic of North Macedonia usually ends up in accounts in places such as Bermuda, Bahamas, Belize, Seychelles, Saint Vincent and the Grenadines, Panama, British Virgin Islands and the state of Delaware in the United States.[141]

A lot of these funds find their way back to the region. According to economists who studied statistics published by the National Bank, most of the foreign direct investments coming into North Macedonia originate from such offshore destinations. In 2018, there was €756 million worth of outflows from North Macedonia, and inflows of €1.17 billion.[142] Large transactions from such offshore countries naturally cause suspicion and experts assume that this is one way that IFFs enter North Macedonia.

It should also be noted that North Macedonia itself, while not a tax haven, does offer preferential corporate tax rates at a flat rate of 10% to attract foreign investment, plus a range of exemptions for permits, VAT, and customs duties. They have facilitated corporate registration in the country, streamlining the Central Register to allow companies to be established within a day.[143] This level of facilitation and speed is unlikely to come without a commensurate reduction in the necessary due diligence to ensure the integrity of such investments.

KEY POINT SUMMARY

- IFFs are generated in the region through multiple forms of corruption and organized crime.
- Corruption-related IFFs can be estimated in the billions of euros, emanating from procurement fraud, graft, bribery and political-party financing violations. Procurement frauds alone divert more than €300 million per year in Albania.
- The three most significant generators of IFFs from organized crime seem to be drug trafficking, illicit trade in counterfeit and substandard goods, and smuggling of migrants.
- Drug trafficking, in heroin and cannabis foremost, followed by cocaine and amphetamines in smaller quantities, is estimated to generate hundreds of millions of euros a year.
- Illicit trade in normally legal goods, of which the best documented is in the tobacco trade, is a well-established illicit industry that caters to international and domestic markets. Its scale is significantly smaller, with the illicit tobacco trade estimated at around €40 million in the region.
- Smuggling migrants through the Balkan route has picked up in recent years, as a result of the crisis in the Mediterranean. Organized-crime groups have profited from the increased demand for migration facilitation across the Balkans.
- Tax evasion is a further component of IFFs, as it circumvents value from the legitimate financial system. A range of schemes are in play to evade taxes, most making significant use of cash transactions and other features of the informal economy, a weak regulatory environment, and offshore tax havens and secrecy jurisdictions.

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CHANNELS OF IFFs

The channels of IFFs are the methods by which illicit flows move value across borders, including money laundering, trade mis-invoicing, cash transfers, and capital account channels. Each channel takes various forms. This chapter considers how, and to what extent, these channels are used to facilitate IFFs in the Western Balkans.

Money laundering

Money laundering is the process by which the proceeds of crime are entered into the legitimate financial system, either nationally or internationally. Martin Navias, a UK lawyer who specializes in finance and security, describes money laundering as 'the inevitable consequence of crimes aimed at profit generation in which the criminal needs to distance himself from the original transgression'.[144] Navias describes how this distancing may be achieved in three phases:

- 'Placement: the illicit proceeds are introduced into the financial system in a way that disguises the true ownership of those funds and seeks to avoid activating the financial industries' anti-money laundering (AML) systems.
- 'Layering: in which there is an attempt to transfer the proceeds of crime through a series of complex financial transactions that serve to disguise the true origins of the funds.
- 'Integration: in which the illicit funds are made to re-enter the economy in an altered character and disguised as legitimate assets.'[145]

According to the 1998 IMF consensus rate, 2–5% of worldwide GDP is circulated as dirty money.[146] In 2009, despite the growth of a formidable AML architecture, the UNODC made a similar conservative estimate of 2.7%.[147] Applying this estimate to the Western Balkans would suggest that €280–700 million is laundered annually in Albania, €155–385 million in Kosovo, and €240–600 million in North Macedonia.

Laundering through construction and real estate

Investment in construction and real estate has a long history of absorbing of illegal monies in the Western Balkans, given that the sector is both meaningful in economic share and poorly regulated.[148] Municipalities across the region provide permits for construction, yet do not have the means to monitor what takes place. Also, for historic reasons, land registries and construction permit records are incomplete and poorly archived.

In Kosovo, the construction and real estate sector generates approximately €1 billion in turnover a year, representing some 8.7% of national GDP.[149] And yet 350 000 buildings built after the war are still without construction permits,[150] and it is fairly common for people to not have ownership papers for their apartments.[151]

In Albania, no private construction was permitted under communist rule and the country suffered from a chronic shortage of housing. Following the collapse of the regime and the transition to a free-market economy in the 1990s, there was a boom in construction both to meet the pre-existing demand and to cater for the surge in rural-to-urban migration. The building of homes and businesses proliferated without zoning regulations, construction permits or proper registration of ownership. A large number of buildings that were constructed illegally between 1995 and 2004 have not yet completed the legalization process.[152] Moreover, construction during the post-communist years was stimulated by people of the Albanian diaspora who chose to invest in Albania, but the source and legitimacy of the funds were almost universally unknown.[153]

Albania's construction boom came to an end in 2012 and, as Figure 10 shows, the number of construction permits issued dropped to negligible levels. With Albania's economic development lagging, few banks were prepared to lend money to an already saturated industry. However, in 2016, the construction sector began to grow sharply, with experts attributing the surge to criminal investment of the proceeds of crime. Sixty-five per cent of all new residential construction permits were issued in the capital, Tirana, with a total investment value of €400 million.[154] Of the 141 companies that received building permits for buildings higher than six floors between 2017 and 2019, 59% did not have the financial capacities to complete them.[155] According to their balance sheets, they had minimal revenues and no assets or loans that would enable them

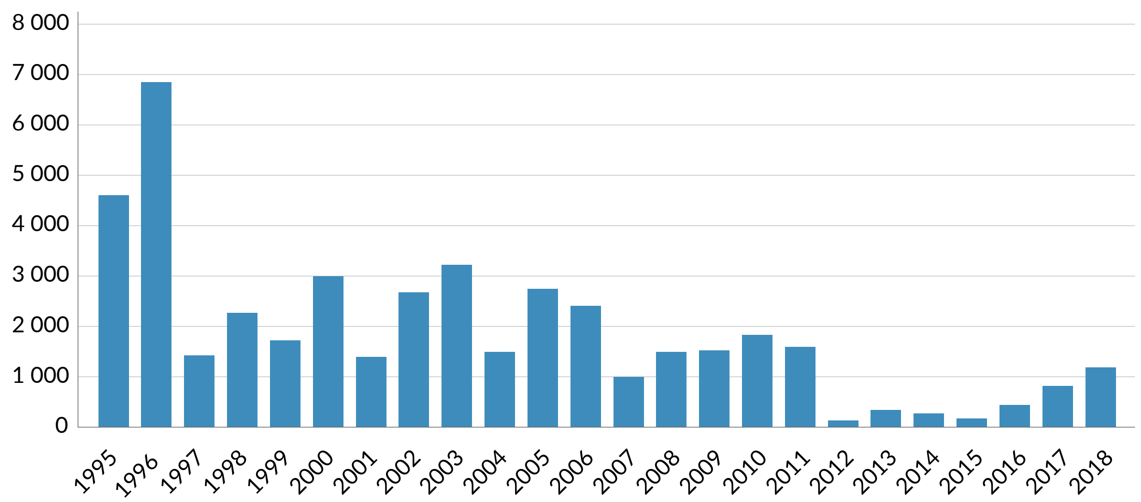

FIGURE 10 Construction permits approved in Albania, 1995–2018

SOURCE: INSTAT, Construction, http://www.instat.gov.al/en/themes/industry-trade-and-services/construction/

The construction sector in all three countries is particularly susceptible to money laundering.

to make such an investment. On our assessment, approximately 60% of this value derives from illicit money, in the region of €240 million.[156]

Mortgage loans can also be used to estimate the scale of money laundering the real estate sector. In 2019, €200 million in new mortgages was issued in Albania. Banks usually finance 50–70% of the apartment value, while the rest is financed through personal savings. This implies that apartments worth €300–400 million were financed by mortgage loans in 2019. Yet, the statistics show that real estate totalling €953 million was constructed, with the difference presumably paid outright by the purchaser or through private loans.[157] A money-laundering expert in Albania estimated that approximately €500 million was laundered through the real estate sector in 2019 in this manner. Using the same calculation for 2017 and 2018 indicates €320 million and €570 million respectively. This adds up to a total estimate of €1.6 billion worth of dirty money laundered through the Albanian real estate sector in those three years.[158]

The construction sector in all three countries is particularly susceptible to money laundering because of the way it is structured. Firstly, new construction almost universally requires clients to pre-pay for the floorplan, which is sold before construction begins. The industry remains largely cash-based, with real estate agents in Albania reporting that 40–50% of all sales are made exclusively in cash. In cases where sales are underwritten by financing agreements, these rarely come from banks or other financial institutions but are instead private loans from other commercial enterprises. The barter system is also sometimes used for new construction, with construction materials being exchanged for finished apartments.[159]

In this fashion, most real estate transactions avoid the scrutiny of the formal financial system or any audit that could flag suspicious transactions. Notaries have previously been seen as susceptible to corruption in Albania, and are now subjected to higher oversight. Since then, they have been cut out of the questionable transactions, and construction companies and real estate agents handle the brokerage themselves. [160]

To front their laundering schemes, criminal groups target construction companies and businesspeople in financially unstable situations who have accumulated debts or loans to repay. They are given large sums of cash to invest in construction projects and purchase apartments, with an informal agreement (usually secured by threats of violence) to hand the apartments back to the criminal group upon completion of the project. Alternatively, illicit money is used to buy shares in the construction company in exchange for apartments given as pay-out upon completion. Mis-declaring the value of the apartment or project allows additional funds to be laundered.[161]

In Albania, the widespread use of illicit money in the construction industry has affected real estate prices. At the end of 2019, the average price of residential apartments in Tirana reached just above €1000 per square metre. This represents a 16% inflation rate from 2016, when the illicit construction boom began.[162] It is also higher than credible in a country where the average monthly income is €420.[163] Numbeo's global cost-of-living database gives Tirana a price-to-income ratio equivalent to those of Milan, Munich and Moscow.[164]

In North Macedonia, the construction of motels for three-hour rentals has created a new way to launder money in the hospitality industry. According to an interview with an adviser of the former prime minister, a motel like that can generate €1.5 million a year in illegal and unrecorded transactions. There are approximately 50 such motels, which would indicate well over €50 million in illegal earnings per year.[165]

In Kosovo, construction is concentrated in the cities of Pristina, Prizren and Ferizaj, but Fushë Kosovë, Lipjan and Gjilan have recorded significant increases. Workers at construction sites reportedly do not have employment contracts – and therefore no official sources of income – but deposit large amounts into their bank accounts, always keeping it below the €10 000 reporting threshold.[166] Several construction businesses are apparently owned by family members or persons close to powerful politicians. Some originally started out in the infrastructure or petroleum-product sectors but reoriented themselves when they were awarded significant public procurement contracts.[167]

Construction in the tourism sector also attracts the kind of big investmesnts that are a money-laundering risk. As in the residential sector, there has been a sharp increase in the number and value of construction permits issued since 2016 (Figure 11).

Criminal groups have established themselves in Albania's most exclusive coastal regions, funding their investments with private loans.[168] Numerous cases illustrate how widely illicit money has infiltrated tourist bars, restaurants, clubs and hotels, especially in the south of Albania. Kosovar politicians are known to invest their kickbacks and corrupt earnings in real estate on the Albanian coast.[169] Media reports from September to November 2019 suggest that the two directors of the land registry office in Vlore were pushed from their posts after being threatened by a well-known local criminal group.[170]

Beyond real estate, the tourism sector and retail sector offer additional opportunities to launder funds into the day-to-day operations of the businesses. Businesses inflate their daily records of sales, meals served or guest numbers, using fictitious high turnover to account for illicit money.[171] While these businesses have been subject to many inspections by the Kosovar Tax Authority for suspected tax evasion, political protection often helps them avoid prosecution.[172]

Money-laundering activities are also facilitated by gaps in the corporate registration process for establishing a limited liability company (LLC). For example, an LLC business can be registered with proprietary capital of €1 000 or even less. After registration, the owner can invest large sums in the business without ever declaring where the money came from. These investments are treated as legitimate expenses, are often tax-deductible, and tax inspectors will not check their origins.[173]

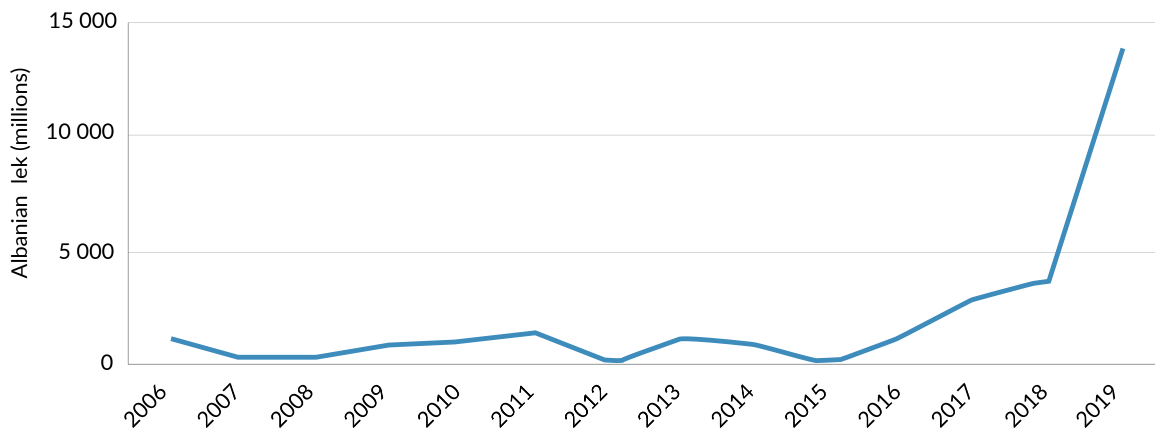

FIGURE 11 Projected funding for the construction of hotels and tourism in Albania

SOURCE: Financial Intelligence Unit of Kosovo, Typologies of Money Laundering and Terrorist Financing in the Republic of Kosovo, 2014, http://fiu.rks-gov.net/wp-content/uploads/2014/10/Typology-Eng1.pdf

Laundering through gambling

Gambling, whether at physical or online casinos, point-of-sale slot machines or sports betting, has long been identified as a money-laundering channel in the Western Balkans. The high cash volume and turnover rate makes for an easy vehicle to commingle dirty money into clean. Gambling is not inherently illegal or wrong, and a well-managed industry can be a boon to the economy through tourism and overseas investment, but without the proper capacity for oversight and regulation, it has high risks for money laundering and the funding of terrorism. From a developmental perspective, gambling is also perceived as a regressive tax on the poor and contributes to the ongoing informality of the economy.

There are multiple methods to launder money through gambling. The most straightforward is for an individual to walk into a casino, buy chips with illicit cash, and then play for a while, preferably on high-odds games. Placing bets on every possible outcome, the bettor will have one or more winners. When cashing in the chips, they will ask for a cheque or at least a receipt so they can claim the proceeds as gambling wins.[174]

Organized crime groups or their associates own casinos expressly for money-laundering purposes. As owners, it is easier for them launder profits through the tellers. The proliferation of on-site betting facilities like slot machines exacerbates this risk, as money launderers can lose all of their cash in the machines and then receive the proceeds as the business owner.[175]

Online betting accounts, which require limited identification verification, offer other possibilities. Money launderers can open an account, make a few small bets, and then cash out the remainder. Establishing dozens of accounts with small amounts keeps the transactions below the threshold that would trigger a suspicious-transaction report. Online gambling is particularly useful for moving money overseas, as funds can be deposited into betting accounts anywhere in the world.[176]

To mitigate the harms of gambling, both Albania and Kosovo banned most forms of gambling in early 2019, including betting shops, slot machines and online sites. In Albania, only casinos in luxury hotels, televised bingo and the national lottery were allowed to continue operations.[177] It had been estimated that Albanians were spending around €700 million on sports betting, of which only €150 million was through legitimate sites. The prime minister stated that the ban was meant to send 'a clear message against organized crime that launders money through this activity'.[178] The opposition party has claimed that illicit money previously laundered through casinos and gambling is now being diverted into construction.[179]

In Kosovo, gambling was also hugely popular, particularly sports betting, and many unemployed young people gambled to 'try their luck'.[180] Before the ban, there were 12 major gambling companies with over 470 partner locations across the country, and the sector was rife with illegal activity. In 2018, the companies had received 700 fines and generated 18 criminal reports, more than 100 slot machines were seized, 28 licences revoked, and 301 locations closed.[181] The industry was dominated by people with ties to high-ranking politicians, and it is alleged that corrupt politicians gambled away the money generated from their illegal activities and then received the laundered income from the gambling business.[182]

A large number of venues that formerly operated as casinos or betting companies have been converted into coffee shops, restaurants and hotels, which are again exploited for their money-laundering potential. Many are used for illegal gambling or to deposit bets for online games. Gambling thus continues, with the government unable to collect tax revenue and criminal groups more firmly in control of the sector. Interviewees reported that the Kosovo police are continually investigating these operations but, due to political influence and corruption, many carry on without trouble.[183]

Gambling is still legal in North Macedonia. With physical betting establishments spread across the country and numerous online sites, the government has shown no indication that it intends to follow its neighbours' example and prohibit gambling.[184] As in Albania and Kosovo, the sector is associated with politically exposed persons and high-level corruption. A 2012 sting operation arrested 23 members of an organized crime family in North Macedonia, including former mayors, relatives of politicians, and members of the country's then ruling party for crimes related to illegal gambling.[185]

Following the bans in Albania and Kosovo, many gambling companies opened subsidiaries in North Macedonia, close to the Kosovo border, or relocated to areas controlled by the NATO Mission for Kosovo (KFOR), such as the village of Karacevo.[186]

Karaceva (also written Karacevo) is a village located at the border with Serbia and is a neutral area, according to the Kumanovo Agreement from 1999. The agreement specifies that there is a 5 kilometre ground safety zone (i.e. neutral zone) by the border, in which KFOR conducts controls and the Kosovo police cannot enter these areas without the permission of the KFOR. Gambling typically attracts criminals from neighbouring countries to launder their money, and limited state oversight over the issuance of gambling licenses facilitates this. North Macedonia is actively developing its tourism industry and it is expected that the gambling ban in Albania and Kosovo will attract more cross-border traffic.

Trade mis-invoicing

The intergovernmental Financial Action Task Force (FATF) recognizes mis-invoicing as one of three principal methods for moving value without physically moving money – and one of the primary channels for IFFs. While there are multiple ways to abuse trade transactions and their financing, the core gambit is the same: the deliberate falsification of the value, volume and/or type of commodity in an international commercial transaction of goods or services, in order to manipulate the value for customs purposes. The differential between actual value and stated value becomes a way of both avoiding tax and shifting large sums of money across international borders. The growth in trade in the globalized economy has amplified the extent and value of trade-based money laundering.[187] An IFF expert from Macedonia believes that this type of 'informal activity' is also stimulated by domestic entities that lack opportunities to place their products in foreign markets.[188]

Under-invoicing of traded products most often occurs at the request of an importer, in order to pay lower import duties. This is also in the exporter's interest, as it reduces the taxable value of the invoice. In most cases, it is a win-win situation for both parties – and a lose-lose for the two states.

Under-invoicing is sometimes also accompanied by illicit cash transfers, where the buyer transfers smaller amounts of money (below the €10 000 reporting threshold) in cash across the border to pay for the goods he receives at lower invoice value than they are worth, as shown in Figure 12.

One indicator of mis-invoicing in international trade is the relationship between income from trade (reflected in the current account deficit) and foreign exchange reserves. In Albania, between 2017 and 2019, the foreign exchange reserves increased by €3.2 billion, from €6.7 billion to €9.9 billion. The trade statistics cannot account for this, showing an increase of only €52 million in 2018, with a similar figure anticipated for 2019 (Figure 13).[189] Experts consulted for this report argue that approximately €3 billion came into the country in ways that are not captured by trade or fiscal data.

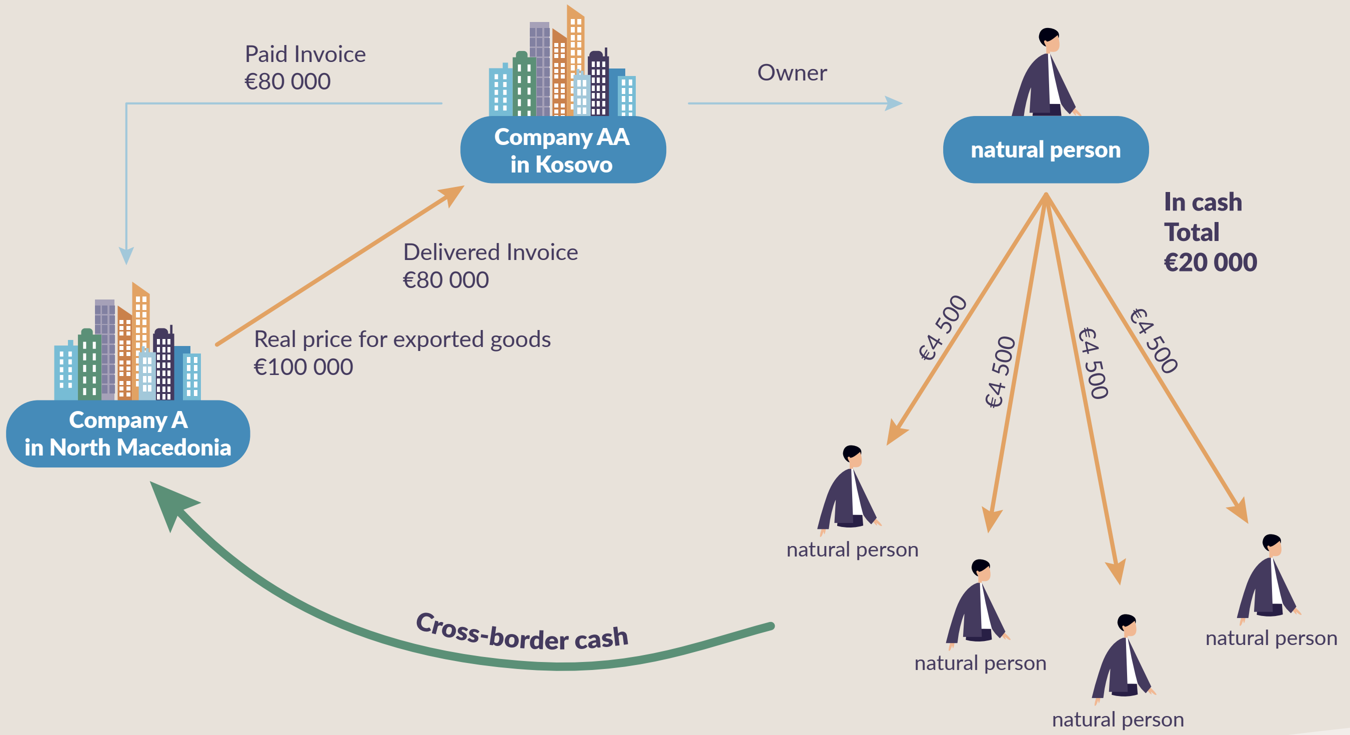

FIGURE 12 Under-invoicing accompanied by illicit cash transfers

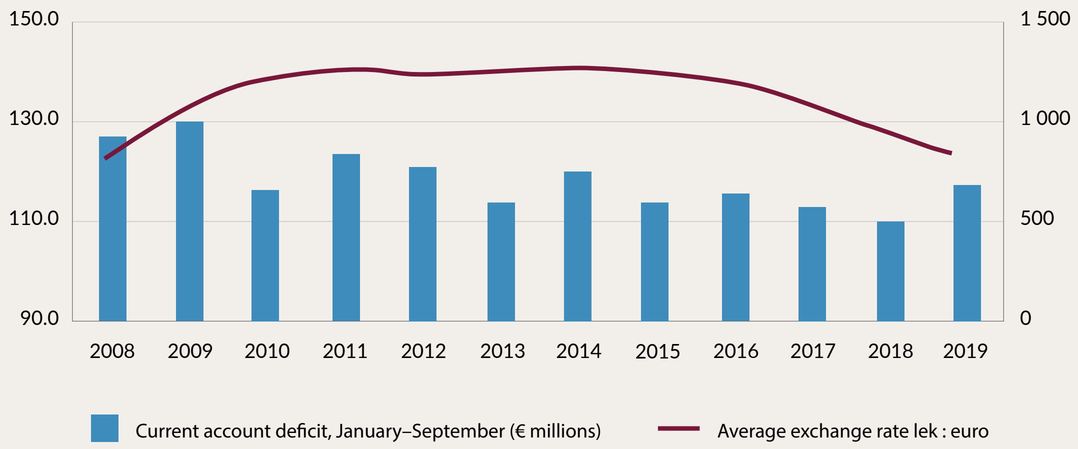

FIGURE 13 Albanian current account deficit (blue) and the average lek:€ exchange rate (2008–2019)

SOURCE: Bank of Albania

The Bank of Albania confirms that more foreign exchange inflows have been observed over the period 2016–2020 than previously. These balance-of-trade discrepancies cannot and should not be attributed exclusively to IFFs, as some may be due to exchange rate fluctuations or other technical volatility. However, the experts believe that up to 80% could be IFFs attributable to drug revenues and mis-invoicing in the trade of goods and services.[190]

In July 2019, the Albanian minister of finance announced a new online invoicing system to reduce tax evasion. The initiative was launched after controls in the hospitality industry discovered 1 600 hotels that were not registered with the tax authority.[191] It remains to be seen whether this will successfully overcome the multiple weaknesses in the monitoring and oversight of trade.

Global Financial Integrity and trade-based estimates of IFFs

Global Financial Integrity (GFI) uses the International Monetary Fund's trade mispricing index to quantify the volume of IFFs leaving developing countries. GFI estimates that around 80% of IFFs occur through trade mis-invoicing.[192]

Their estimation is based on two criteria: mispricing of trade and balance-of-payment leakages. To arrive at these values, GFI conducts a trade/value gap analysis, examining the differential between a country's stated imports and exports and the import and export balances in the countries of origin and destination. This methodology implies that the entire differential can be accounted for by trade mis-pricing with criminal intent.

GFI does not provide any data for IFFs in Kosovo, but it does for North Macedonia and Albania.

GFI's analysis for North Macedonia suggests that illicit outflows during 2004–2013 were US$516 million per year, with a sharp peak in 2008, where their estimate is closer to US$928 million. The statistics show that almost 97% of this money was sent out of North Macedonia through fake invoices that increased the value of export/import goods and services.[193]

In Albania, the GFI estimate suggests that US$123 million was lost through trade mispricing from 2004 to 2012, and again shows a peak in 2008 of US$305 million. The cumulative estimate from 2008 to 2017 equals US$5.5 billion. From 2013 to 2017, import under-invoicing and export over-invoicing represented some 21.8% of the country's total trade volume. This is high, even when compared to other developing countries.

GFI's methodology has been widely criticized because it includes goods with listed market values along with tangible goods that have abstract values (such as artworks) and intangible goods (services).[194] Mis-invoicing is particularly difficult to ascertain where prices are not quoted or determined by any catalogue value.

Despite the criticism, however, the approach does offer analytical value. As GFI states in its own defence: whether or not trade mis-invoicing is an appropriate proxy for IFFs in their entirety, few would dispute that it is a substantial illicit outflow with severe development consequences. It is also the selected metric that underpins SDG 16.4, the Sustainable Development Goal related to IFFs.

Cash transfers

Cash smuggling is another straightforward channel for moving value illicitly, particularly within cash-dominant economies, such as those of the Western Balkans, with large informal financial sectors.[195] In this context, illicit actors can effortlessly extract, move and absorb large amounts of value without leaving a trace in the formal financial systems, and it is consequently challenging to even begin to estimate the scale of such flows.

The majority of cash transfers happen simply by driving cars across the border, mainly at official checkpoints. With little to no control at the border posts, and many of them unmanned most of the time, crossing the border with cash carries little risk. Police and customs officials in Kosovo, for example, acknowledge that they focus on stopping illicit goods and drugs from crossing the border and pay limited attention to cash entering and leaving the country.[196] However, the amount of cash that is seized by officials gives some indication of the scale. In one prominent case in June 2018, Albanian customs officials at the port of Durres seized €3.4 million in a trailer coming from Belgium.[197]

The Customs Administration of North Macedonia recorded annual totals of several million Euros worth of foreign currency seized at border crossing points between 2011 and 2019.[198] The main border crossings for currency smuggling in North Macedonia are Bogodorica, Tabanovce and Skopje International Airport, and most of the funds were seized from Macedonian nationals, followed by foreign nationals from neighbouring Greece, Serbia and Kosovo, as well as Turkish nationals. Cash was most frequently seized from Macedonian nationals on exit from the country, while the foreign nationals were caught about equally entering and exiting.[199]

Cash couriers travel regularly between Albania and EU countries and the UK, carrying no more than €10 000 each way to avoid suspicion. Members of criminal groups ask relatives, friends or other Albanians on holiday to carry money back home in exchange for a small commission. Spain was identified as a particular base for cash couriers to Albania.[200] According to a senior anti-smuggling official from the Albanian Customs Administration, loopholes have been created to enable the transfer of cash into the country. 'For example,' he explained, 'if you get caught with €50 000, it is sufficient to pay a €500 fine for non-declaration and leave with the money. This is possible as the law is not very explicit.'[201]

Powerful businesspeople working in Albania, Kosovo and North Macedonia carry significant sums of cash between the countries.

Cash-smuggling cases are rarely reported in the media because they are not considered newsworthy. North Macedonian statistics show that, between 2010 and 2015, more than €150 million was declared at exit, entry or transit border crossing points, but there is a decreasing trend in declarations of foreign currency at the borders.[202] The origins of this amount of cash cannot be determined with certainty but, declared or not, there are grounds for suspicion. Individuals who do not declare their cash holdings are already skirting the law, while those who do declare must have some reason for carrying large amounts of cash rather than using bank transactions and the fast money-transfer facilities of the formal financial system.

Powerful businesspeople working in Albania, Kosovo and North Macedonia carry significant sums of cash between the countries. In an interview, a customs officer

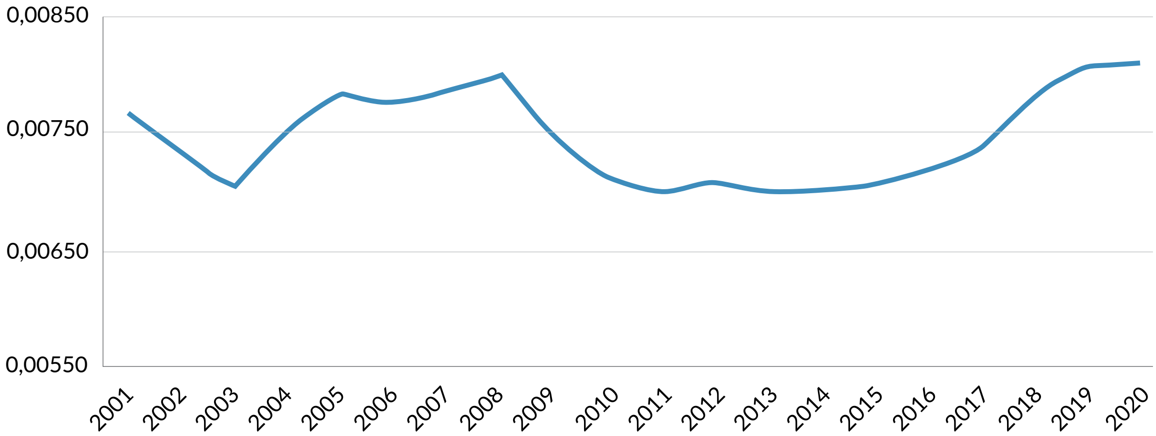

FIGURE 14 Foreign currency exchange rate, ALL:€ (2001–2020)

SOURCE: Oanda, Currency Converter, https://www1.oanda.com/currency/converter/

referred to a businessman who is suspected of transporting cash between Albania and North Macedonia, as he has investments in both countries. The officer said, 'No one dares to check the trunk of his car because of how powerful he is. Nobody would stop him and control his car.'[203]

Organized criminal groups use their distribution networks to transport drugs across Europe and to bring the proceeds back to Albania. Cash is reportedly transferred across the border in the trucks of import/export companies and cars with hidden compartments. An Albanian source explained that this is the preferred method to bring proceeds of crime into the country: 'Trucks that carry goods make it easier to hide the money. Truck drivers usually get paid by distance, but they do not get a decent paycheque. They therefore use the extra space to also transport cash.'[204]

The commission for the driver ranges from 8 to 15% of the total cash being transported, and at least 10% if cash is to be transported out of London. The interviewee explained that the 'London boys' pay extra because they tend to have a lot of cash available. This money may have been legitimately earned, but most Albanians working in London do not have a residence permit and are paid in cash. The money is then entrusted to individuals with EU passports who carry it slowly across the borders and back home as remittances for the family.[205]

When asked what channels politicians use to move cash abroad, an Albanian customs officer answered, 'Very simple: it is enough to cooperate with a general director of customs whose car is not controlled when crossing the border. This is usually the case in Greece. The money is transported in cash and deposited in offshore banks through legal channels.'[206]

Currency exchange services

A range of schemes use currency exchange to move value illicitly, and the scale of such fraudulent transactions may have triggered an artificial appreciation in Albania's currency since 2016.

Albania's exchange rate is determined in a free-floating currency regime. Having been stable for about six years, from 2010 to 2016, the Albanian lek began to noticeably appreciate against the euro (Figure 14) and a basket of different currencies. Arguing that this cannot be explained by movements in the formal economy alone, some experts believe it is the result of channelling illicit money into Albania.[207]

In 2019, Albania's trade balance deficit increased by €195 million, approximately 40% more than in 2018. This deficit should ordinarily have weakened the lek in relation to the euro, but instead, the currency appreciated. Interlocutors from the Bank of Albania attributed this to unusual inflows of currency – 19.2% higher in 2019 than in the previous year.

Simultaneously, foreign-currency savings in Albania increased: in January 2020, 54.7% of all deposits were held in foreign currency, compared to 50.6% in January 2016.[208]

Currency exchange bureaus have played a major role in circulating dirty money. New foreign exchange offices have proliferated in the past few years, with 58 registered in Albania alone in 2018. The total turnover of all foreign exchange offices was about €73 million in 2018.[209] The offices are legally entitled to buy and sell currency in accordance with their capital, but they also buy and sell money on behalf of client accounts, with transactions of up to €2 million per day.[210] According to one market operator, this is not only against the law but transactions at that scale can have a direct impact on the exchange rate. It is also believed that some currency exchange offices give short-term, high-interest 'shark loans' to businesses.[211]

North Macedonia offers a window into another channel for potential cross-border cash transfers and foreign exchange manipulation: fast money transfers. The country has nine fast-money-transfer service providers, using three global electronic money-transfer systems (Western Union, MoneyGram and RIA). Six of the service providers are banks, while the other three operate legally under a permit issued by the National Bank of the Republic of North Macedonia (NBRNM). These services are mostly used by the diaspora to transfer money to their relatives living in North Macedonia, and their use is on the rise.

Fast money transfers are negotiated in two currencies: euros and US dollars. North Macedonia's Law on Fast Money Transfer Services sets a €2 500 daily limit per person for sending and a €5 000 daily limit for withdrawing, and service providers are obliged to notify the tax authority of all transactions over €1 000 at the end of each business day.[212] NBRNM issues permits according to precisely defined criteria, and the Bank and the Financial Intelligence Unit supervise lenders and subagents. But in reality, these compliance measures are poorly maintained and easily susceptible to fraud on the sending side, as local agents can be manipulated to exceed the individual sending limits.[213]

Credit card fraud

North Macedonian customs officials cited credit card and ID fraud as another means of carrying value across borders undeclared. Foreign nationals use forged IDs and payment cards to buy expensive items, technical equipment (cell phones, computers) or jewellery, which can then be worn or carried as personal items across the state border and converted into cash.

Capital account channels

Not all of the funds that run through IFFs begin with a predicate crime. Some are earned legitimately, quasi-legitimately or informally but then become illicit when transferred in contravention of national or international laws. This can entail tax evasion, trade mis-invoicing, cash transfers and other schemes.[214] These transactions can make use of the infrastructure of the global financial system, benefitting from the growing architecture of secrecy jurisdictions that obscure the origin and destination of illicit flows.

As we have seen, criminal proceeds from drug trafficking are generated in the EU and invested at home and around the world. Corrupt politicians and elites, enriched through crime and graft, transfer their wealth into offshore accounts. The Panama Papers leak revealed scores of Western Balkan individuals, and companies linked to Western Balkan countries, holding considerable wealth offshore.[215]

Many of the people interviewed for this report also referred to the importance of the internet and cryptocurrencies like bitcoin to move money illicitly in and out of the region and across the Western Balkan countries. There is little evidence thus far to substantiate these claims, and it is difficult to estimate how widespread these techniques are.[216]

It is clear from the evidence presented that there is extensive laundering of illicit money into the legitimate economy in each of the three countries. It is invested into political parties or laundered through real estate, construction, retail and a host of other sectors domestically, within the region, and further abroad.[217] But it is the flows from beyond the region that typically attract the most attention.

Flows from beyond the region

Funds from the diaspora and criminal enterprises beyond the region are sent back and laundered into the Western Balkans economies. This money is often used to interfere with local political and electoral processes, as witnessed by repeated claims of illegal campaign financing, external donors underwriting candidates, and 'black suitcases' of illicit money changing hands, despite nominal legislative steps taken to improve electoral integrity.[218]

To give one example, the Serbian Public Prosecutor's Office for Organized Crime ordered an investigation into transnational fraud including abuse of office, tax evasion, and money laundering between 1 January 2015 and 14 December 2017. Of the 36 people accused, 16 have been arrested. These individuals established four legal entities in Serbia and one in London. In North Macedonia, they opened non-resident bank accounts. Serbian legal entities received money from several legal entities that were registered in the Serbian Business Registers Agency based on false invoices for services rendered. Subsequently, they transferred approximately 518 million Serbian dinars (about €5 million) to non-resident accounts in North Macedonia. Members of the group went to North Macedonia, withdrew the money, and transferred it to Serbia in individual amounts of less than €10 000. The members of the criminal group then returned the funds to the companies from which they were obtained, charging a commission of between 6% and 10%, thus accruing illegal profits of around €400 000, and causing about €800 000 damage to Serbia's budget.[219]

KEY POINT SUMMARY

- IFFs are moved into, across, and out of Albania, Kosovo and North Macedonia through four main channels: cash transfers, trade mis-invoicing, money laundering and capital accounts.
- While money laundering is often considered a proxy for IFFs generally, it is rather the process by which the proceeds of crime are entered (layered) into the legitimate financial system.
- Construction and real estate, gambling, and trade were identified as the most significant sectors to launder money in the three countries. Using mortgage loans data, an expert calculated that approximately €500 million was laundered through the real estate sector in Albania in 2019 alone.
- Although gambling was banned in Albania and Kosovo at the beginning of 2019, there are many reports of continuing gambling operations and of companies opening subsidiaries in North Macedonia, where gambling remains permitted. Some Kosovar companies have also relocated their activities to KFOR-controlled military areas.
- Under-invoicing of goods and services, which minimizes the payment of taxes and allows for money laundering, is a common practice in Albania, Kosovo and North Macedonia.
- Cash smuggling is also one of the most straightforward means of moving value illicitly. Due to the large informal sectors, transactions are usually made in cash in the Western Balkans. Cash is mostly smuggled in private cars or trucks driving across the border, often in hidden compartments.
- Currency exchange services and credit card fraud are other ways to move value illicitly.
- IFFs that extend beyond the region attract the most attention, such as organized criminal groups generating illicit money in the EU and laundering it into the Western Balkan economies. Individuals and companies linked to the region reportedly hold considerable wealth offshore.

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ASSESSING RESPONSES TO IFFs IN THE WESTERN BALKANS

This section of the report considers the progress that has been made in establishing appropriate legal, regulatory and enforcement mechanisms to counter IFFs.

Any assessment of the efforts of these countries to counter IFFs should begin with the clear understanding that this is not an easy challenge to address, and on a global scale there are few – arguably no – countries that can say with confidence that they are succeeding. As the previous sections have attempted to demonstrate, IFFs exploit every weakness of state institutions while simultaneously eroding their foundations in governance, integrity and the rule of law.

The overarching concept of illicit financial flows, with its lack of definitional clarity and the very broad net it casts, is not yet very helpful when it comes to designing technical response frameworks. The battle proceeds on many fronts – organized crime, corruption, poverty, inequality and financial exclusion – none of which is straightforward or easily won. It is also a transnational problem that requires collaborative solutions. Differential legal and tax regimes, and the existence of tax havens, free trade zones, and secrecy jurisdictions all undermine national responses and create perverse incentives for IFFs. The success, or lack thereof, of the Western Balkans should be understood in this context.

Illicit actors shift across the region in response to national changes in the legal framework and its enforcement. The 2019 ban on gambling in Albania and Kosovo, for example, saw companies relocating to North Macedonia to continue their activities.

Payments and money transfers related to smuggling activities are realized in cash, offset in other goods, or even exchanged with each other in complex webs of seemingly borderless, frictionless value transfer. Police officers from Kosovo described how the situation of villages along the borders – including those controlled by KFOR and thus beyond the jurisdiction of the national police – is exploited to smuggle contraband.[220]

The political imperative to address IFFs comes as a prerequisite for EU accession. The enlargement perspective for the Western Balkans requires progress on the rule of law and competitiveness and reducing the levels of corruption and organized crime. Noting that 'the region's economies are uncompetitive, with too much undue political interference and an underdeveloped private sector', the enlargement perspective also points to

> elements of state capture, including links with organized crime and corruption at all levels of government and administration, as well as a strong entanglement of public and private interests. All this feeds a sentiment of impunity and inequality. There is also extensive political interference in and control of the media. A visibly empowered and independent judiciary and accountable governments and administrations are essential for bringing about the lasting societal change that is needed.[221]

The EU acquis prescribes a clear set of standards and targets that each of the Western Balkan countries would need to meet before membership could be considered,[222] and the countries have committed to do so. In March 2020, the European Commission agreed to open accession negotiations with both Albania and North Macedonia, as the key conditions had been met.[223]

The EU and its member states have accordingly invested in initiatives to build the capacity of relevant state institutions. While these rarely have the explicit objective of addressing IFFs – unsurprisingly, given that the concept is still quite new – the elements of money laundering, organized crime and corruption are all well codified and on point. In addition, efforts to reform economic governance and to modernize the legal framework often include elements that are key to fighting economic crime and IFFs.

For example, the EU funded a UNODC project to build regional mechanisms for anti-money laundering and countering the financing of terrorism (AML/CFT) in south-eastern Europe. The project, which ran from December 2017 to 2019, supported national capacities to conduct financial investigations and to cooperate in international AML programmes.[224] GIZ also has a programme for countering serious crime in the Western Balkans that supports financial investigations, prosecutions and the recovery criminal assets. [225] Its global programme on combatting IFFs, which approaches the topic holistically, also includes the Western Balkans as a priority region. This targets intervention and prevention at several levels, including transparency of ownership issues, risk assessments for money laundering, and adherence to AML/CTF standards.[226]

The measure of overall efficacy can perhaps be taken from successfully completed prosecutions for related offences. However, as the 2019 European Commission report on EU accession concludes,

> overall, track records of final convictions in organised crime cases often remain weak. Some countries can only demonstrate a handful if any final convictions for organized crime or money laundering in recent years. Such poor results show the ineffectiveness of criminal procedures, give strong signals of impunity, and contribute to the risk of criminal infiltration of the political and economic systems. Countries also need to increase significantly the seizure and confiscation of assets in both organised crime and corruption cases, and to tackle criminal groups more forcefully.[227]

Anti-money laundering

Criminal groups and the corrupt may be the instigators, but the money-laundering ecosystem is enabled by a wide host of financial, legal and commercial professionals, whose services help to obscure illicit money, or who fail to question the provenance of their clients' funds. The challenge of effectively combatting the problem is intensified by the diversity of sectors and financial instruments utilized. The global estimate is that less than 1% of all proceeds of crime laundered into the economy are seized and/or frozen annually.[228] Even the FATF, the custodians of the established AML architecture, have acknowledged its weaknesses, prompting a global rethinking of its one-size-fits-all approach.[229]

In the ecosystem of corruption and impunity in the Western Balkans, however, the AML regime's emphasis on exactitude and technical compliance rings particularly hollow. Albania, Kosovo and North Macedonia's institutions have introduced national AML legislation and coordination mechanisms and have bolstered their financial intelligence capacity. Their considerable investments and effort in modifying legal frameworks, generating suspicious-transaction reports (STRs) and promoting other compliance measures in the formal financial sector – measures that have already demonstrated their inefficacy globally – have been rendered even more futile against the extensiveness of the informal sector, the weakness of regulatory bodies, and the prevailing levels of corruption and impunity in these countries.

ALBANIA

According to the MONEYVAL reports,[230] Albania has made significant progress since the introduction of the country's first AML law in 2000. The country has created an AML agency and a special anti-corruption prosecutor's office. It introduced several laws in recent years, in parallel with EU directives. Working with organizations such as MONEYVAL, Albania has continually increased the criminalization of money-laundering and terrorism-financing (ML/TF) activities and introduced a comprehensive vetting process of judges.[231] Based on this progress and reforms, the EU opened accession negotiations with Albania in March 2020.

On 17 May 2000, Albania introduced its first AML legislation (Law No. 8610). It included a definition of money laundering and prevention mechanisms for monitoring and reporting of ML activities. In parallel with the law, the Money Laundering Coordination Agency (MLCA) was created under the Ministry of Finance.

Three years later, on 19 June 2003, the parliament approved a revised AML law (No. 9084). Most notably, this required all entities to register all transactions over 2 million leke and to report any suspicious transactions below that value. Additionally, the law lowered the value of transactions that need to be automatically reported from 70 million to 20 million leke. There were also structural changes to the MLCA.

On 19 May 2008, the Law on the Prevention of Money Laundering and Financing of Terrorism (No. 9917) marked a transition from AML legislation to AML/CFT. The law created a requirement for entities to use client-identification documents in financial relationships. Additionally, it set out monitoring requirements for the purchase of gambling chips over 200 000 leke and single transactions of more than 1.5 million leke. Law No. 9917 was amended three times, two of which imposed minor changes. The second amendment, in 2015, made changes that adapted to EU Directives 2015/849 and 2018/843, in line with MONEYVAL recommendations.

With regard to terrorism financing, Law No. 157 was passed on 10 October 2013 and the Criminal Code was amended in 2014. More specifically, these changes expanded the criminalization of engagement in foreign fighting and related acts such as recruitment and financing. In February 2020, Albania made a high-level political commitment to work with the FATF and MONEYVAL to strengthen the effectiveness of its AML/CFT regime. The monitoring process will last for two years, with an emphasis on the fields where the country was found either low or moderately compliant with the FATF 40+9 Recommendations. As a result, Albania was grey-listed.

KOSOVO

Kosovo has implemented laws in accordance with EU directives and has created relatively compliant money laundering definitions according to the FATF and MONEYVAL recommendations. However, the provisions of the AML/CFT laws are still not clear enough to allow easy adjudication by the courts. The definitions need careful review to remove ambiguities and ensure straightforward comprehension in Serbian and Albanian.

In September 2004, the Financial Intelligence Centre (FIC) became operational, following UNMIK's Regulation on the Deterrence of Money Laundering and Related Criminal Offences (2004/2). This regulation went through minor amendments in 2005 (Regulation 2005/9) and twice in 2006 (2006/9, 2006/53).

The AML system was introduced in Kosovo in 2008, the year it declared independence. At this time, the FIC was handed over from UNMIK to the European Union Rule of Law Mission in Kosovo (EULEX).

In 2010, the Law on the Prevention of Money Laundering and Terrorist Financing (No. 03/L-196) was adopted, by which the FIC was replaced by the Financial Intelligence Unit of Kosovo (FIU-K). It also stipulates measures, competent authorities, and procedures for detecting and preventing ML/TF activities. In 2013, a supplementary law (No. 04/L-178) changed minor details of the 2010 law, such as definitions and wording.

A four-year plan to combat the informal economy and financial crimes (including AML/CFT measures) was drafted in 2014. Additionally, an FIU-K Administrative Instruction (No. 05/2014) set out the minimum standards, written procedures, and controls for AML/CFT. Minor changes were made to Kosovo's AML/CFT laws in 2015 (FIU Administrative Instruction Nos. 02/2015 and 03/2015, respectively). 2016 saw the adoption of a significant AML/CFT law (No. 05/L-196). Its purpose was to implement EU Directives 2015/849 and 648/2012 and repeal Directives 2005/60/EC and 2006/70/EC. FIU-K Administrative Instruction No. 02/2017 was adopted in 2017, which provided for AML/CFT training.

In 2019, a second four-year plan was created for 2019–2023. It sets out a national strategy for preventing and combatting the informal economy and financial crimes (including AML/CFT).

However, Kosovo's efforts to combat money laundering have stagnated, with only 11 people indicted for money laundering and four found guilty.[232] The government's strategy to combat the informal economy involved a campaign to increase the rate of invoicing for commercial transactions. It directly provided businesses with fiscal cash registers, which drew widespread criticism due to the high cost of the items themselves, and the potential monopoly created by the government procurement.[233] An outreach campaign offered citizens monetary rewards for collecting and submitting the fiscal coupons issued by the registers to the Tax Administration. Regrettably, a large number of businesses that were equipped with fiscal registers refused to issue the coupons and maintained the registers only to fulfil the legal criteria. The campaign thus far has had limited impact, and there seems little political will to impose a stricter implementation of measures against the informal economy.

NORTH MACEDONIA

The Republic of North Macedonia has improved its AML/CFT legal framework in line with EU directives and FATF recommendations. North Macedonia joined MONEYVAL in 1998, and the Egmont Group, an international platform of financial intelligence units to combat ML/TF, in June 2004. The MONEYVAL committee concluded that the country was able to fulfil all required recommendations in the 2014–2018 period and withdrew North Macedonia from regular progress reports. Based on this progress and reforms, the EU opened accession negotiations with North Macedonia in March 2020.

In 2001, North Macedonia adopted its first AML law (No. 70/01). Three years later, a new law was needed to better comply with international legislation. The new law (No. 46/04) came into force on 20 July 2004.

In 2002, the Financial Intelligence Office (FIO) was instituted under the Ministry of Finance. The FIO collects, processes, analyzes, stores and submits ML/TF information.

Law No. 4/08 was adopted on 10 January 2008. Shifting focus from AML to AML/CFT, it introduced crucial measures against terrorist financing, to better comply with the nine special FATF recommendations. This made it obligatory for banks to use AML software that enabled the government to better analyze suspicious transactions. Additionally, banks were required to complete more stringent client analyses prior to engaging in financial activities.

Perhaps the most significant law today (No. 120/18) was adopted on 26 June 2018 as an amendment to previous AML/CFT laws. This allowed North Macedonia to implement the measures necessary to cohere to EU Directive 4 (2015/849) and part of EU Directive 5 (2018/843). Several complementary guidelines (186/2018, 243/2018) were also adopted by the ministry of finance and the FIO prepared other documents to provide instructions and methods to facilitate AML/CFT. Another draft law to further align with EU AML Directives 5 and 6.

The Criminal Code of the Republic of North Macedonia (2009, amended 2018) also has several AML articles. The 13 clauses of Article 273 set the sentences for a wide range of money-laundering activities, including fines, prison terms of up to 10 years, and seizure of the income or property gained in the crime. Article 98a states that, for an ML crime with a four-year or longer prison sentence, any property of the convicted that was acquired in a period prior to conviction and that exceeds their legal income will be confiscated.

The last MONEYVAL evaluation report in 2019 deemed the country to be partially compliant. It concluded that, between 2014 and 2018, North Macedonia had fulfilled the required recommendations and that its legal framework was in line with FATF recommendations and, consequently, EU Directives.[234]

While the total number of crimes committed in North Macedonia has decreased in recent years, the government argues that there is a constant increase in the crimes that generate criminal proceeds.[235] Nevertheless, between 2013 and 2015, only five criminal groups were indicted with the criminal felony of money laundering.[236]

Limitations

Important gaps remain in these apparently comprehensive legal and oversight frameworks, and the adoption of good laws by no means guarantees their successful implementation. During the course of the research for this study, legal provisions were often criticized for not being clear and straightforward enough for prosecutors and judges to understand and work effectively with when cases are presented.

Ironically, members of the judiciary in Kosovo observed that, due to the preponderance of international assistance, clauses that may be clear in English are not so well articulated in Albanian or Serbian. This creates a lot of room for interpretation, particularly in the lower courts where fluency in English is less common.[237] Similarly, North Macedonia's Law on Prevention of Money Laundering and Other Proceeds of Crime, as amended in 2018, is now 160 articles and 75 pages long. This complexity compromises its potential to be effectively understood and applied by the criminal justice system.

In addition, the law introduced a mandatory national risk-assessment to be conducted at least every four years, in order to demonstrate the country's efforts towards 13 defined objectives.[238] The first assessment was completed in 2016 and an updated one is expected in June 2020.

Experts also indicated that the legal and regulatory frameworks suffer from being fragmented between different state institutions. In North Macedonia, for example, the supervisory bodies include the Financial Intelligence Office, the National Bank of the Republic of North Macedonia, the Insurance Supervision Agency and many more. The state bodies authorized for prosecution are the Ministry of the Interior, the Financial Police Office, the Customs Administration and the Public Prosecution Office for Organized Crime and Corruption. Still other anti-money laundering regulations are embedded in Macedonian criminal and banking law.

The previous sections of this report documented numerous examples of fish slipping through the net that is meant to catch them, and the apparent annual volume of IFFs remains significant. For example, strong evidence confirms that the construction sector is commonly used to launder money in Albania, Kosovo and North Macedonia, and yet this risk is not often addressed within the AML mechanisms.

This suggests that, despite its apparent comprehensiveness, the legal framework is undermined by remaining loopholes and weaknesses in implementation that compromise the countries' abilities to achieve their goals.

Financial regulation

Albania, Kosovo and North Macedonia like to put forward their procedures for suspicious transaction reports (STRs) to demonstrate their efforts to decrease IFFs. Suspicious transactions are reported by individual institutions and submitted to the General Directorate for the Prevention of Money Laundering in each country, where the data is gathered and published in an annual Suspicious Activity Report. As shown in Figure 14, they have all been steadily increasing their rate of STR filing.

The latest data available for all three countries comes from 2017, but an interviewee from Albania's FIU reported a total of 1 525 suspicious transactions in 2018, an increase of 10.2% from the previous year.[239] Numbers have been increasing steadily in all three countries, although at a much faster pace in Albania and Kosovo. As Figure 15 shows, North Macedonia significantly lags behind the other two.[240]

However, the filing of STRs is only one indicator of compliance and it does not speak to the effectiveness of the system. An explosion of STRs could indicate a weak filtering system that is generating too many alerts – many of which might be false positives. The burden of assessing excessive reports can overwhelm weak compliance systems and regulatory bodies.[241]

Another clear weakness highlighted by the research is that the institutions responsible for identifying and preventing the entry of crime proceeds into the financial system do not quantify them. Annual reports from the three countries typically list the number of cash transactions, but not their volume or size. With this data, it is impossible to determine how much cash enters and is withdrawn from the financial system. Investigative authorities charged with identifying the proceeds of crime also do not quantify these.

Reporting entity or industry	2017		
	Albania	Kosovo	North Macedonia
Banks	686	10	177
Money transfer companies	165	5	526
General Directorate of Customs / insurance related	46	15	1
General Directorate of Taxation	5	n/a	n/a
Lawyers	n/a	840	1
Central Office for the Registration of Immovable Property	83	n/a	n/a
Exchange bureau	n/a	41	n/a
Game of chance / gambling	n/a	42	2
Public notaries	254	74	23
Real-estate agencies	n/a	46	n/a
CEOs	20	n/a	n/a
Dealers in precious metals and stones	n/a	411	n/a
Non-bank financial institutions	10	11	2
Auditors	n/a	20	n/a
Car dealers	101	n/a	n/a
Other	14	n/a	n/a
Total	1 384	1 515	232

FIGURE 15 Overview of suspicious transaction reports in Albania, Kosovo and North Macedonia (2017)

SOURCES: Council of Europe, Assessment report on compliance of Kosovo with international anti-money laundering and combating the financing of terrorism standards, 2018, https://rm.coe.int/assessment-report-on-compliance-of-kosovo-with-international-anti-mone/16809381e1; Albanian Financial Intelligence Unit, The General Directorate for Money Laundering Prevention, Annual Report 2018, http://fiu.gov.al/wp-content/uploads/2019/RaporteVjetore/Annual_Report_2018.pdf; Ministry of Finance (North Macedonia), Annual Report 2018, http://www.ufr.gov.mk/files/docs/Godisenizvestaj2018.pdf.

In North Macedonia, for example, there is no legal limit on the amount of cash that can be deposited into the financial system by a natural person or legal entity. Each bank chooses its ceiling and follows internal procedures and rules for flagging transactions this as suspicious.[242] In most cases, the minimum threshold for STRs is €10 000.

Anti-corruption efforts

Overall, chronic corruption continues to undermine the narrative of progress in the Western Balkans. As cited above, the EU found that weak rule of law, state interference in the economy, weak financial regulatory capacity and abuses in areas of public procurement have left the space for IFFs wide open. Frequent changes in the regulatory and taxation policies create ambiguities and loopholes that the criminal and corrupt do not hesitate to exploit.[243]

In 2018, the Western Balkan countries made public anti-corruption pledges in alignment with the 2016 Global Declaration Against Corruption.[244] These included wide-ranging commitments on public procurement, asset recovery, and anti-corruption education, among others.[245]

However, a recent civil-society review of those commitments observed that, despite a ‘dynamic and exponential’ increase in legislation, and multiple visible gestures towards addressing corruption and promoting transparency, honesty and accountability, there has been no fundamental increase in integrity. Notable omissions on critical issues – such as access to information, party political financing, public procurement, conflict of interest and illicit enrichment – leave a legislative framework with no teeth to take on the most egregious violations.

As with the anti-money laundering framework, what happens in practice doesn't rise to the aspirations of what exists on paper. Many acts of corruption are not reported, many reported cases are not processed, and too many are dropped by the prosecution or reluctantly brought to the courts only to be dismissed. For the relatively few convictions, sanctions often fall below prescribed minimum sentences. Despite well-crafted strategies and policies (often developed with international prompting and assistance), the lack of political will ensures that they do not achieve their stated goals.[246]

Another pertinent limitation identified by the civil society review was that the recently-established anti-corruption bodies in the Western Balkans are generally given mandates restricted to prevention, awareness-raising and capacity-building, rather than independent oversight and investigation. Albania, for example, which does not have a dedicated anti-corruption agency, splits the responsibility for implementing the national anti-corruption strategy between a national coordinator seated within the ministry of justice and a pluri-ministerial coordinating committee: thus not allowing for operational independence from the government. Another common challenge has been the creation of specialized anti-corruption law enforcement, prosecution and judicial benches. These regularly come into jurisdictional conflict with the regular criminal justice bodies, prompting competition and politicization.[247]

To summarize: in the various strategies designed to reduce the hazards of corruption, organized crime and money laundering in the Western Balkans, the technical compliance is high enough to reach the bar set for EU accession, but little has changed in the political economy of the Western Balkans, and this is the change required for tangible progress. This, in turn, suggests that an IFF lens could make an important contribution to the debate, as its holistic, development-centric approach can potentially revitalize these long-standing efforts.

KEY POINT SUMMARY

- The IFF ecosystem is sustained by a wide host of financial, legal and commercial professionals whose services are employed to help obscure illicit money. The diversity of sectors targeted intensifies the challenge of effectively combatting the problem.
- Progress has been made in establishing appropriate legal, regulatory and enforcement mechanisms to counter IFFs in Albania, Kosovo and North Macedonia. However, this progress was largely achieved on paper with slow implementation by the authorities and little impact on local realities. Numerous examples show that illicit actors quickly respond to changes in enforcement or the legal framework and arbitrage among the countries.
- The countries often point at the increase in STRs filed over the last years as a measure of improvement of their AML efforts. STRs have increased in all countries – although at a much faster pace in Albania and Kosovo. However, the filing of STR reports is only one indicator of compliance. Money-laundering-related convictions remain low across the region.
- The bodies in charge of anti-corruption efforts are fragmented and it is often unclear which is in charge. Also, their mandates are restricted to prevention, awareness-raising and capacity-building rather than enabling them to perform independent oversight and investigations.

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POLICY IMPLICATIONS

IFFs represent a fundamental constraint to development in the Western Balkans. A culture of permissiveness and impunity erodes the seemingly positive progress that the three Western Balkan countries are making towards EU accession, economic growth and democratic governance. In the past twenty years, the capacity to divert, protect, extract and grow state resources and criminal rents for personal enrichment has warped citizens' concept of the state and the rule of law.

The wide scope of the IFF agenda, which simultaneously considers the components and channels of IFFs, the broader political economy of their context and the effects of their flows, as well as the technical and administrative requirements to combat them, can be a game-changing framework for action. The Western Balkans has the benefit of international political commitments, support, resources and investment potential. As the countries move closer towards EU accession and as key technical benchmarks have been met, the issue must now be to break down the prevailing status quo of vested interest and elite enrichment in an environment of corrupt political economy.

Agendas on anti-corruption, countering organized crime, preventing money laundering and addressing challenges of poverty, inequality, informality and economic exclusion need to be brought together, and policies and programmes coordinated for maximum efficacy. The IFF debate is an effective framework to provide that coherence and coordination, as it promotes prioritization on the forms of IFFs that are most harmful to development.

Considering IFFs post-COVID-19

The majority of the research for this report was undertaken before the COVID-19 pandemic and the resultant controls applied on movement both internally and at the borders. At the time of writing, in June 2020, all of the Western Balkan countries have had their borders closed since March and have significantly restricted the movement of people.[248] Law-enforcement and security capacity has been diverted towards policing civic behaviour to limit the spread of infection, supporting the delivery of urgent medical supplies, and measures to prevent social unrest. Crimefighting has fallen down the priority list.[249]

From GI-TOC's monitoring of the illicit economy, via the civil-society SEE-Obs platform, it is clear that measures taken to control the pandemic have also impacted the operations of criminal groups, and the local dynamics are changing.[250] Human-smuggling markets dropped significantly as movement was restricted and borders closed. No new arrivals of migrants or refugees have been recorded in the three countries of study since the lockdown began in mid-March.[251] Drugs are still moving: cannabis production has risen slightly, but heroin supplies are reportedly scarce due to constraints higher up the supply chain. Distribution to local markets is ongoing, though with greater friction, which is reflected in the street prices.[252] Analysts predict that criminal groups may shift their manufacturing and logistics to smaller towns and rural areas to reduce their visibility to law-enforcement agencies. In Tirana, the number of arrests related to drugs is second only to curfew violations.[253]

Regarding IFFs, we can presume that the border controls have also impacted the cross-border movement of cash, which normally travels with local border-crossing people. Given the extent to which this illicit flow often feeds into local remittance economies – particularly in Kosovo, where remittances represent a massive portion of national GDP – this will exacerbate the economic shock of the pandemic on the population. While informal-sector beneficiaries of the cash-transfer economy may suffer, criminal groups that use cash couriers and cash transfers for money laundering are likely to quickly shift to other forms of value transfer. In a context where urgent medical supplies, foodstuffs and humanitarian goods are being sent quickly across the continent, and customs officials are being told to expedite their passage,[254] opportunities for illicit trafficking and trade and trade-based money laundering are expanding dramatically.

Experts have also expressed concern that actors with large amounts of illicit cash will have enhanced leverage when liquidity starts to dry up in the private and public sectors. Entrepreneurs in Albania have already warned about the possibility that companies declaring bankruptcy amid the COVID-19 crisis might be used for money-laundering purposes.[255]

Criminal scams began almost immediately in the region, as has price-gouging on personal protective equipment (PPE) and critical medical supplies. Fake doctors are allegedly making targeted calls to the hospitals, trying to sell medical supplies at extremely high prices; websites with similar offers have proliferated.[256] The bigger share of the pie will come with state procurement for PPE and other opportunities for corruption in procurement in the health sector. Fraud and corruption will be a risk

for any economic stimulus packages developed to offset a long-term economic contraction in the region.

Moreover, there are serious long-term concerns should the pandemic persist in the Western Balkans. In an environment of weak institutions, criminal groups may position themselves as partners to official authorities, offering to deliver services, distribute assistance or provide support to communities where the state is unable to do so.[257] Failures in state service-delivery could fundamentally compromise the fragile trust that citizens of the region are developing in the integrity and capacity of state institutions. More egregious breaches of public trust and human rights, in the form of heavy-handed securitization of public-order policing or border enforcement, could reawaken the barely dormant legacies of recent conflicts, and significantly set back democratization. Another concerning development since the pandemic began is an increase in attacks on the media in Albania, which will compromise the fourth estate's investigative and oversight functions.[258]

The pandemic is unquestionably a major disrupter and the post-COVID-19 scenario needs to be carefully monitored. Changes to the local, national and regional political economy will have to be factored in, as the landscape will likely be fundamentally altered. Responses to IFFs will also need to be reconsidered, and new opportunities may present themselves to change longstanding paradigms and incentives.

Protesters in Kosovo's capital, Pristina, observe social distancing ahead of a court ruling, May 2020. *© Armend Nimani/AFP via Getty Images*

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CONCLUSION

This report assessed the regional dynamics of IFFs in the Western Balkans, with a focus on Albania, Kosovo and North Macedonia. While the national risk assessments, the mutual evaluation reports by MONEYVAL, and the EU progress reports provide detailed analyses from a state-level perspective, this report presents a complementary civil-society view of issues raised during interviews in the field from December 2019 to March 2020. It uses examples and case studies of how illicit monies are earned, transferred and laundered in the three countries and transnationally.

The growth and scale of IFFs in Albania, Kosovo and North Macedonia clearly benefit from the region's interconnectedness and integration. The geographic location makes them a transit route, where commodities, people and financial flows can easily cross borders. The criminal and the corrupt use these advantages to arbitrage around the region, placing their assets and investments where it suits them best to do so.

Drug trafficking, human smuggling and illicit trade are the key organized-crime activities that generate illicit funds. Most prominently, the involvement of Albanian organized criminal groups along the supply chain of the international cocaine trade reportedly generates significant criminal profits in the region. However, less-profitable forms of organized crime also have an important impact on the local economy and society, and should not be discounted.

Wider regional and transnational politics are also at play, with criminals from neighbouring countries moving their illicit goods around the region, and assuming that lax oversight will allow them to invest and launder their profits with impunity. Despite the imposition of anti-corruption and transparency measures in all three countries, corruption remains both a principal source of IFFs and the largest obstacle to preventing them. The wider perception, of both this report and international monitors, is that government authorities are working harder to roll back the measures to increase transparency and accountability, and to weaken systems of checks and balances, than to strengthen integrity and the rule of law.

Trade mis-invoicing, e.g. particularly under-invoicing of goods and services, was also identified as one of the principal methods to transfer IFFs. It often occurs at the request of a foreign importer who asks his partner to report the exported goods below value in order to pay lower import duties. For example, the 'imbalance' between the income from trade and foreign exchange reserves which can currently be observed in Albania is assumed to be the result of trade mis-invoicing.

Numerous accounts point to the transfer of cash as the most important channel to transfer illicit money across borders, whether in concealed compartments of cars or hidden among licit products in transport trucks. However, there is little understanding of the volumes entering and leaving the countries. With the exception of Albania, there is no evidence of how much people earn smuggling cash. The entry of Illicit cash into the licit local economies is facilitated by the wide-spread use of cash and the large informal economies of Albania, North Macedonia and, particularly, Kosovo. The cash economy also facilitates IFFs in various ways in different formal sectors and industries.

Illicit monies that are not smuggled out into offshore accounts are laundered locally, notably into electoral finances and the construction and gambling industries. Particular opportunities related to real estate and the tourism industry were identified in Albania, and the gambling sector in North Macedonia, which is the only country where gambling remains legal and operates with limited oversight and political protection.

One important conclusion of this report is that, although Albania, Kosovo and North Macedonia have a sound legislative AML/TF framework and have joined numerous international conventions aimed at combatting IFFs, many institutions lack the capacity to implement these laws and guidelines in practice. National risk assessments and MONEYVAL mutual evaluation reports show that the countries have a solid understanding of their risks, but loopholes, inconsistencies and fragmentation, along with weak capacity and corruption, undermine their implementation.

While the number of STRs has continuously increased, the number of successful prosecutions and convictions related to IFFs (especially money laundering) remains shockingly low. Improvements have indeed been made on many fronts, but most convictions are for predicate crimes and not money laundering directly, and the completed prosecutions are a token of the estimated scale of offences. There is also a need to focus on tracking money laundering and recovering stolen assets. More could be done on a national level to improve cooperation among institutions, particularly in terms of enhancing cooperation between law-enforcement agencies, both in the Western Balkans and internationally. What is missing is, again, is practical cooperation.

Civil society actors have a key role to play in responding to IFFs in the Western Balkans. They should continue to push for effective governance and institutions and a culture of lawfulness. They can work with governments to prioritize issues related to the most damaging flows. At the same time, the international community needs to pressure the governments of the region to ensure space and freedom for the media, NGOs and concerned citizens to express their opinions.

IFFs in the Western Balkans remain understudied. More data and research will be needed to achieve a regional understanding of the phenomenon and to include Bosnia and Herzegovina, Montenegro and Serbia. Enhanced discussions and debates among all stakeholders can improve understanding of the key drivers and trends that enable IFFs in the Western Balkans, thus opening opportunities for stronger responses.

National conclusions

While the general conclusion above applies to all three Western Balkan countries, some distinctions are worth highlighting.

ALBANIA

Drug trafficking has been the most important profit centre for criminal groups in Albania for the last 30 years. Cannabis cultivation remains strong in various areas of the country, despite significant efforts to curb the production since 2014. Cannabis generates illicit profits along a value chain that extends from the villagers who cultivate the crops to the organized criminal groups who smuggle and sell it across the EU. However, the profits from cocaine trafficking are far higher, reaching €20 000 per kilogram.

Following narcotics trafficking, corruption and graft is the second leading source of IFFs in Albania. Recent investigations show that €300 million is lost annually to abuses in public procurement procedures, which would be nearly 45% of the total bid value of public contracts awarded in 2019.

Corporate crime and tax evasion are also significant in Albania. Experts suggest that nearly 80% of the imbalance between trade income and foreign exchange reserves can be attributed to over-invoicing relative to the actual value of goods and services entering the country.

Large parts of these illicit proceeds are transferred by cash in and out of Albania. Cash remains the most straightforward means of moving value, particularly in a country which has historically been sceptical towards the banking system. Organized crime groups use their distribution networks and cash couriers travel regularly between EU countries, the UK and Albania, carrying no more than €10 000 one way, in order not to attract suspicion. It is reported that cash is often transferred across the border in trucks of import/ export companies and cars with special compartments. The commission for truck drivers ranges between 8% and 15%.

Currency exchange offices are used extensively in Albania for illicit money transfers, with 58 new offices registered in 2018 alone. Experts argue that the noticeable appreciation of the Albanian lek since 2016, which cannot be explained by movements in the formal economy, is the result of channelling illicit money into the country.

The Albanian gambling industry was also at particular risk for money laundering. To counter this, the government banned all forms of gambling in 2019. However, the opposition party claims that illicit money has since been diverted into the construction and real estate sector, which has long been associated with money laundering. The industry continues to be largely cash-based, commonly using the barter system as form of payment and using pre-payments as initial sources of funding. In fact, the wide-spread use of illicit money in the industry has already affected real estate prices, especially in Tirana where the average price of residential apartments reached just above 1000€/m^2 at the end of 2019. In addition, experts point out that of 141 companies which received permits to construct buildings of six floors (and higher) between 2017 and 2019, 59% do not show the financial capacities to complete them.

Growing attacks on the media in Albania are a concerning development, in particular since the pandemic, and that will compromise the capacity of the fourth estate to perform its investigative and oversight function.

NORTH MACEDONIA

IFFs in North Macedonia are strongly influenced by the country's role as a transit route for people and commodities moving between Asia and Western Europe. While political scandals and the name dispute with neighbouring Greece had long hampered North Macedonia's path towards EU accession, efforts have recently been recognized by officially opening negotiations in April 2020.

The most significant predicate-crime component of IFFs in North Macedonia is corruption and abuse of power, with government statistics suggesting that the number of such crimes is steadily increasing year on year. Despite widespread anti-corruption efforts, corruption remains highly prevalent at transactional levels such as bribery, which should be the easiest to eradicate. This suggests an almost cultural tolerance of pervasive corruption and the weak rule of law.

Money channelled out of North Macedonia usually ends up in accounts in tax havens and secrecy jurisdictions with low taxes and no obligation to disclose the ownership of bank accounts. Bogodorica, Tabanovce and Skopje International Airports are the border crossings where the most incoming foreign currency has been seized.

Fast money transfers are another channel for moving illicit funds in North Macedonia. The National Bank issues permits for these service providers and, along with the Financial Intelligence Unit, is responsible for the supervision of lenders and subagents, but compliance measures are poorly maintained and susceptible to fraud.

Reports suggest that trade-based money laundering is particularly common. Local companies under-invoice export products and cash is smuggled across the border in return. Non-resident accounts, which are opened specifically for paying invoices, work similarly.

Other money-laundering methods include life-insurance policies where instalments are paid in cash. The gambling industry is a particular concern, especially after it was banned in Albania and Kosovo and companies relocated their operations to North Macedonia. While the country is generally aware of the risks, it is also developing its tourism industry to accommodate more traffic from Albania and Kosovo.

KOSOVO

Kosovo's unresolved international status, which impedes its accession to various international organizations, has significant influence – not least because it limits the information available on the topic.

Proceeds from corruption and abuse of power are believed to be the largest component of IFFs in Kosovo. Road construction is reportedly one of the sectors most susceptible to public-procurement corruption. For example, there are several accounts of tender violations in the Gjilan highway project and others. Organized criminal groups are active in a wide array of money-generating activities, particularly drug trafficking and human smuggling. Migrants enter the country from both directions: from the south heading towards Serbia and the EU, and from the north to Albania and Italy.

Facilitated by the country's geographic location, its porous borders and the disputed area in North Kosovo, Kosovo is a hub for smuggling of counterfeit goods and illicit trade, notably cigarettes. The goods often leave the country at 'alternative' crossing border points, usually in the mountains or other rugged terrain. Organized criminal groups from Kosovo have joined with larger criminal networks across the Western Balkans producing and smuggling cigarettes, with further connections to the Middle East.

Money-laundering channels in Kosovo continue to be largely cash-based. Businesses are reported to inflate their sales and profits to account for illicit funds, to use fictious companies to escape paying taxes, and to mis-invoice goods and services for international trade.

The gambling industry is another high-risk sector for money laundering. Although gambling was banned in 2019, a large number of former casinos and betting companies have been turned into coffee shops, restaurants and hotels where the gambling and money laundering continues. Other gambling operations relocated to KFOR-controlled military areas where the police cannot enter without permission.

As in Albania, money is laundered through the construction and real estate sector. Several construction businesses are reportedly to be owned by the family members or close associates of powerful politicians. Businesses pay their employees in cash, and the employees make large cash deposits into their bank accounts. However, illicit money generated in Kosovo is not only laundered through the local construction industry: Kosovar criminal groups also appear to be investing in real estate at the Albanian seaside.

RECOMMENDATIONS

As we have emphasized throughout this report, layering an IFF agenda over ongoing but sometimes siloed anti-money laundering and anti-corruption efforts could revitalize those conversations and provide for better integration and coordination in a more holistic approach. The coronavirus pandemic amplifies that potential.

Following the OECD best practice guidelines to address IFFs, recommendations are offered in four key areas.[259]

1. IDENTIFY AND RAISE AWARENESS OF THE TYPES, MAGNITUDES AND RISKS OF IFFS.

As noted, 'illicit financial flows' is a relatively new development-oriented concept that is not in wide use in the Western Balkan countries. Its novelty can help to open fresh dialogue opportunities with state officials, the private sector, civil society and the general public. It could frame participatory conversations focussed on understanding and mitigating development harms.[260] Such consultations would be able to promote local interests in a debate that is often perceived as externally driven. The role of civil society here is key: they should be actively involved in assessing risks and presenting people's experience of IFF activities and the threats posed to democracy and peace. Civil-society perspectives should also be included when assessing impacts and prioritizing responses.

The paucity of current evidence limits the potential of IFFs as a policymaking imperative. The full range of risks and harms of IFFs are often not appreciated, particularly where people seem resigned to institutionalized corruption, impunity, poverty and informality.

They may themselves depend on or benefit from informal and illicit flows, which can make acknowledging, detecting and combatting IFFs even more difficult.

There is a significant need to increase the quantity and quality of data available on the magnitude and nature of IFFs and to ensure that they are transparently available and generally accessible to the general public. It is worth noting, for example, that some of the public information requests submitted in the course of this study received no response over the nine-month project period. The regular publication of business information and corporate registers of both domestic and foreign corporations and trusts operating in the region is essential.

From these consultations, a national risk assessment and strategy could be produced. These should clearly understand and articulate the main sources, destinations and channels of IFF inflows and outflows, and their domestic and regional impacts.

The post-COVID-19 landscape may be fertile ground for emphasizing IFF questions: the harmful impacts of crime and corruption will come into sharper focus as criminal groups exploit economic need and human vulnerability, and the venality of political corruption (particularly in the healthcare system) will be acutely apparent. Civil society engagement and investment will be key to harness this.

2. CONSIDER THE CONTEXTUAL FACTORS THAT ALLOW IFFS TO THRIVE.

Responses to IFFs need to consider the non-policy drivers that can strengthen or weaken their effectiveness. This includes addressing questions about the state of the economy, the availability of resources to counter IFFs, and regional and international levels of integration that might hamper domestic action.

The extent of informality is clearly a significant driver of IFFs: it reduces oversight of financial transactions and hides the full scale of resource-diversion. It allows for the proceeds of crime to be easily concealed and blocks effective financial investigations, thereby compromising the capacity of the criminal justice system to hold criminals to account. Informality also exposes populations to health, safety and exploitation risks, and leaves them without safety nets when wages are paid in cash. Without considerable efforts to address informality, most other IFF agendas will remain largely ornamental.

Again, the response to the pandemic may offer opportunities to address informality and financial inclusion. Large-scale economic stimulus or other social welfare programmes may provide the opportunity to register and transition informal sector workers into the formal economy. This will enhance the capacity for oversight and regulation of the economy and reduce space for IFFs.

The post-COVID-19 economy may also mobilize a groundswell of public momentum and political will to address the IFF enablers of chronic inequality and enrichment. For example, the government of Poland and other countries are leading an initiative to deny access to government stimulus packages to companies that have registered offshore in tax havens and secrecy jurisdictions.[261] The Tax Justice Network (TJN) has also proposed a five-step 'bail or bailout' test to guide government thinking on eligibility criteria for government assistance, to enhance tax transparency for bailout money, and to prevent taxpayers' money from being siphoned into corporate tax havens. Governments are asked to consider whether a company requesting a bailout has registered subsidiaries in the highest ranked countries on the Financial Secrecy Index or the Corporate Tax Haven Index; whether it has been involved in any of the financial leak scandals, such as the Panama Papers; whether it transparently publishes its financial accounts, and not only for national entities but for all the legal entities in the group; whether there is clear information on beneficial ownership; and finally, whether the company is prepared to commit to employee protection and to no shareholder extraction until the bailout has been repaid.[262] The countries of the Western Balkans could apply these tax-responsible rules to promote overall reform to corporate transparency and to reduce the risk of public subsidies joining in with IFFs.

The TJN also has recommendations for reducing the risks in public procurement processes, such as automatically barring tax-dodging companies.[263] Given the scale of public procurement expected to result from the economic response to the pandemic, national and EU regulations could be amended to prevent such companies from taking part in public infrastructure projects or in public-private partnerships.

3. CONSIDER CRITICAL INTERACTIONS ACROSS ECONOMIC, SOCIAL AND ENVIRONMENTAL AREAS TO ADDRESS IFFS (HORIZONTAL COHERENCE).

In all of the Western Balkans countries, there is clearly a lack of internal coherence in the fight against IFFs. The different initiatives that would comprise the response (anti-money laundering, financial investigations, international cooperation, anti-corruption) have also been addressed in a relatively piecemeal fashion, with different ministries and departments leading different aspects. This has resulted in major loopholes between legal frameworks, enforcement, judiciary, taxation and fiscal strategy. More broadly, lines of leadership are unclear and departments do not work coherently together. This has contributed to the sense that political will is lacking, and that impunity continues for illicit flows and economic crimes.

Senior leadership and advocacy, ideally in a non-partisan manner, is key to linking this fragmented terrain together. Those appointed to lead must be able to work with operational independence, sufficient resources, and internal and external political support.

Focus must be given to reporting entities, in particular to designated non-financial businesses and professions such as lawyers, notaries, real estate agencies and professionals in other sectors that are vulnerable to money laundering. Awareness raising, capacity building and monitoring for compliance will be a key requisite in the fight against IFFs. This includes civil society, investigative journalists, and other bodies with the capacity to provide civilian oversight.

Other governance weaknesses undermine the fight against IFFs. Exposing corruption and illicit activity requires an active media and civil society. The Western Balkan countries are known for the lack of independence in the media, and recent years have seen rising efforts to threaten journalists and activists working on sensitive areas. Promoting and protecting civic action and independent media reporting will need to be part of the broader strategy.

4. SUPPORT COHERENCE WITHIN AND BETWEEN NATIONAL AND INTERNATIONAL NORMATIVE FRAMEWORKS (VERTICAL COHERENCE).

Due to the nature of IFFs, any country would be hard-pressed to fight them alone. Global efforts need to be joined to tackle this transnational issue. It requires regional and international harmonization, and cooperative and coordinated action, particularly within the EU enlargement process and the Berlin Process. Most efforts in the fight against IFFs have thus far been directed to put pressure on the Western Balkan countries to meet international standards of compliance, mutual assistance, international cooperation, and asset seizure. However, far more effort is needed in the other three pillars of response outlined above before the impact of strengthened vertical coherence can be felt.

Discrepancies in tax policies and enforcement capacity within the Balkan region create space for criminal actors to manoeuvre. Tax havens and secrecy jurisdictions globally create the means, and increase the incentives for, corruption and money laundering. These weaknesses will have to be addressed.

The growth and scale of IFFs in Albania, Kosovo and North Macedonia benefit greatly from the region's interconnectedness and integration. Yet IFFs in the Western Balkans remain an understudied phenomenon. More data and research will be needed to achieve a cross-regional understanding of the phenomenon and also to investigate the countries' links to Bosnia and Herzegovina, Montenegro and Serbia. Enhanced discussions among all stakeholders can raise awareness of the key drivers and trends that enable IFFs in the Western Balkans, and better comprehension of the phenomenon will open possibilities for a framework upon which stronger responses can be predicated.

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