Latvia as a Shadow-Economy Offshore Financial Centre in the Age of Anti-Money Laundering

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Abstract

This thesis explores the impact of the Financial Action Task Force (FATF) regime on the geography of illicit offshore finance, using a Foucaldian governmentality approach, for the case of Latvia. Latvia is the only post-Soviet financial centre to have been implicated directly in the illicit financial flows of the 1990s, but which after 2000 went on to join the North Atlantic Treaty Organisation (NATO), the European Union, the Eurozone and the Organisation for Economic Cooperation and Development (OECD), while satisfactorily adopting FATF rules. How did FATF effect illicit financial flows via Riga after 2000? Based on interviews with Latvian and international bankers, regulators, investigators and observers, as well as digital data mobilised from surface, deep, social and dark webs, this thesis describes the development of a banking sector in Riga that was defined by its being de jure onshore, de facto offshore. Latvia had none of the regulatory identifiers of an offshore financial centre such as low tax rates and high levels of corporate secrecy, ringfenced for non-residents, and boasted a high level of compliance with FATF rules. But at the time of gaining independence from the Soviet Union it radically deregulated its banking sector, opening it to offshore shell firms holding dollar deposits on behalf of customers from other former Soviet states. Latvia's being effectively whitelisted by FATF and OECD after 2000 lent legitimacy to such money, while political protection for the offshore banking sector informally exempted it from anti-money laundering (AML) laws. Dollar payments routed via Riga between the post-Soviet shadow economies and the US correspondent banking system soared after 2000. In the case of Latvia, the geography of financial legitimacy described in the indices of the FATF regime legitimised undeclared funds from the post-Soviet shadow economy. The proliferation of indices of financial legitimacy was thus grist to the money launderers' mill. The need to combat illicit offshore financial flows that undermine democracies remains urgent.

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List of Common Abbreviations

ABS	Advanced business services
AML	Anti-money laundering
AML-CFT	Anti-money laundering - combating financing of terrorism
CIS	Commonwealth of Independent States (Russia, Belarus, Ukraine, Moldova, Armenia, Azerbaijan, Kazakhstan, Kyrgyzstan, Uzbekistan, Turkmenistan)
BIS	Bank for International Settlements
BoNY	Bank of New York
BVI	British Virgin Islands
CBR	Central Bank of Russian Federation
EMI	Electronic money institutions
ESRC	Economic and Social Research Committee
FATF	Financial Action Task Force
AML	Anti-money laundering
FCMC	Financial and Capital Markets Commission
FinCEN	Financial Crimes Enforcement Network
FIU	Financial Intelligence Unit
OFC	Offshore financial centre
IMF	International Monetary Fund
KYC	Know your customer
LLP	Limited Liability Partnership
Moneyval	Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism
NBU	National Bank of Ukraine
OCCRP	Organised Crime and Corruption Reporting Project
OECD	Organisation for Economic Cooperation and Development
USSR	Union of Soviet Socialist Republics
PEP	Politically exposed person
SLP	Scottish limited partnership
SWIFT	Society for Worldwide Interbank Financial Telecommunication
USA PATRIOT ACT	Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act
USRCD	Unified State Register of Court Decisions of Ukraine

Chapter 1. Introduction

It is well established that corruption is a threat to democracy, but just how direct the link is became clear in August 2020, when Russian anti-corruption campaigner and opposition politician Aleksei Navalny nearly died after being poisoned, apparently on orders of the Russian authorities, while he was campaigning in the West Siberian town of Tomsk. Navalny had made his name with investigations of corruption among Russia's elite, including president and prime minister, that he published as videos on the internet (NY Times 2020a). Navalny's widely watched investigations often reflected on the role played by offshore shell firms as vehicles for Russian corruption. Thus an investigation in 2017 identified close friends of incumbent prime minister - and former president - Dmitry Medvedev as proxies for Medvedev in controlling a Cyprus company that owns a 17^{th} century villa vineyard in Tuscany and two luxury yachts (NY Times 2017). Navalny's own investigations into his poisoning established that it was carried out by Russian secret service operatives on Kremlin orders (NY Times 2020b).

In the reverse scenario, just weeks before Navalny's poisoning, former Malaysian prime minister Najib Razak was sentenced in Malaysia to 12 years for his part in a major corruption case. 1 Malaysia Development Berhad (1MBD) was a Malaysian sovereign wealth fund set up by Najib Razak after his election as prime minister in 2009 to support foreign investment. According to an indictment by the US justice department, more than $4.5bn was stolen from 1MBD and moved into accounts in Switzerland, Singapore and the United States. Around $731mn arrived on Najib's personal accounts (Guardian 2018c, Guardian 2020b). Highlighting the threat to democracy from corruption, when the Malaysian Anti-Corruption Agency started investigating corruption allegations concerning 1MDB and the prime minister, Najib fired top officials who had backed the investigation, including the attorney general, appointing loyalists in their place to clear his name. Nevertheless, confronted with public outrage over the corruption allegations Najib lost a bid for re-election and was arrested (Guardian 2020b).

While Malaysia shows how corruption creates threats to democracy, it also shows that democracy can check corruption. The case of Azerbaijan shows how a patrimonial dictatorship uses offshore finance both to steal public money, but also to legitimise an aggressive authoritarian foreign policy by channelling secret payments to foreign political figures, influencers and PR projects. The ‘Azerbaijani laundromat’ refers to a pipeline of secret offshore payments totalling around $2.9bn paid to beneficiaries in Germany, the UK, France, and Turkey between 2012 and 2014 (Guardian 2017c). Some of the money appeared to be payments to current and former European parliamentarians, other money went to individuals close to the regime, including kickbacks from arms suppliers in Russia and Israel (Guardian 2017c). The money helped build up a foreign policy platform conducive to launch military hostilities again the ethnic Armenian minority in Nagorno-Karabakh in autumn 2020.

Brazil’s *Lava Jato* (Car Wash) investigation uncovered over $5bn paid to company executives and political parties, leading to a wave of arrests that undermined Brazil’s democracy (Guardian 2017b). Directors of Petrobras, Brazil’s largest company, were found to have overpaid on contracts for construction work, drilling rigs and auxiliary vessels and refineries. The markup was diverted into secret accounts that were then directed to politicians and parties who had appointed the Petrobras directors. Large sums were deposited in Swiss bank accounts (Guardian 2017b). The judge overseeing the investigation died in suspicious circumstances (Guardian 2017b). One administration that refused to stop the investigation was ousted by those threatened by the investigation, but the successor administration then fell under impact of the investigation (New York Times 2019). The linkage between offshore finance, corruption and endangered democracy again held true.

Democracy was also endangered by South Africa's President Jacob Zuma’s allegedly corrupt relationship to the Gupta family of and their parent company Sahara Group during his presidency 2009-2018 (BBC 2018a). The Guptas were accused of exercising extensive political influence in South Africa in an egregious case of “state capture” whereby the Gupta family would select candidates for ministerial posts. Democracy was also endangered when the Gupta family hired a leading British PR firm to discredit critics as representatives of “white monopoly capital” (BBC 2018a). After losing power, South Africa’s high court ordered an investment firm linked to the Gupta family to repay US$41 million siphoned off from the state electricity company and spun through a web of 10 shell companies mostly in Bermuda and consulting firms banking at South African and international banks (OCCRP 2019b). South African authorities have said they are looking to recover around $4bn from Gupta-linked structures and offshore accounts.

All these cases feature different combinations of offshore finance, corruption and threats to democracy. In the rest of the introduction, I will consider the relationship of offshore finance, corruption and democracy when formulating the research question for this thesis, outlining my argument, and introducing the case study. Finally, I will outline the thesis structure.

1.1 Research question

Since offshore finance facilitates corruption, and corruption is anti-democratic, offshore finance is potentially anti-democratic. However, since offshore finance cannot be tackled on the national level alone, it is widely accepted that the anti-corruption campaign must be coordinated internationally:

> Without similar international policy responses to tax havens, secrecy jurisdictions and other forms of complicity in money laundering operations, national level initiatives to prevent corrupt financial transfers risk being hamstrung. In fact, it is arguable that the development of transnational corruption networks, with their links to both international crime and to terrorism, represent the most urgent challenge the anti-corruption movement faces (Heywood 2017 p36).

The Financial Action Task Force on Money Laundering (FATF) was established in 1989 by the Group of Seven (G7) intergovernmental organisation (comprising USA, UK, Canada, Japan, Germany, France and Italy) to tackle the illegal narcotics trade. Two years later, the collapse of the Soviet Union and the emergence of 15 very weak successor states plunged one sixth of the world's surface area into a vortex of lawlessness, corruption and illicit offshore financial flows (Handelman 1995). By 2002 the International Monetary Fund reported that the "profound and far-reaching transformations" resulting from the Soviet collapse involved "the most chaotic economic, political, and social changes in modern history" rife with "rent seeking, corruption, and outright thievery" (Abed and Gupta 2002 p3). This dollarisation and offshorisation of a major, formerly closed, economy significantly fuelled the global offshore economy and the problem of money laundering (Farah and Braun 2007). Flows of dirty money had become the new normal over much of the globe (Heywood 2017).

Against this background, in 1996, FATF's key recommendation on criminalisation of money laundering was expanded beyond drug money laundering to include all crimes (FATF 1996). FATF established a toolkit for countries to implement anti-money laundering (AML) policies domestically and coordinate internationally: Mutual Evaluations, Financial Intelligence Units

(FIUs), and most controversially, blacklists and greylists of countries failing to adequately combat money laundering, thus risking sanctions. But as the cases above indicate, despite the introduction of the FATF regime, money laundering scandals have continued and even proliferated. There is thus wide criticism of FATF for ineffectiveness. At the same time, critics have argued that FATF has created a financial surveillance regime that violates privacy, while being itself unaccountable (Verhage 2011).

My research question is therefore how has the FATF regime impacted on the geography of illicit finance? To tackle this question, I use a diachronic case study of one financial centre, tracing its development from before the implementation of FATF rules to after. It makes sense for such a case study to examine post-Soviet offshore finance, given the "signal importance" of the collapse of the Soviet Union for the anti-corruption agenda and the expansion of FATF in the 1990s (Heywood 2017 p22, Sharman 2017). A qualitative study is required because the object of examination is the quality of money, whether 'dirty' or 'clean'.

To answer this question, I examine the case of Latvia, a former Soviet republic on the Baltic Sea, specifically the offshore financial sector in its capital Riga, which until 2018 handled US dollars for clients mostly incorporated as offshore shell firms. Riga is the only financial centre to have moved from being first part of the Soviet Union, then implicated in the illicit financial flows of the 1990s, to joining the EU and NATO by 2004, the Eurozone by 2014 and the OECD by 2016, in the process adopting AML institutions and practices. This makes it an optimal test case for the impact of the FATF regime on illicit offshore financial flows.

Following the collapse of the Soviet Union in 1991, Riga boasted as many as 50 banks handling dollars for non-resident clients. Latvia was affected by the overall lawlessness of the post-Soviet aftermath, and money laundering by the banks in Riga was a widely recognised problem (Jonsson, and Karrstrand 2007, Galeotti and Bowen 2014, Jemberga, and Purina 2016, Delna 2018). In 1995, when Latvia's largest bank collapsed after mass theft of deposits and transfer of assets abroad, the bank was discovered to have been owned and run by an organised crime group. However, when Latvia and the other Baltic states were fast-tracked for EU and NATO membership starting 1995, they also committed to introducing anti-money laundering legislation and institutions in compliance with the standards developed by FATF (Jonsson, and Karrstrand 2007, Galeotti and Bowen 2014). The legislation and institutions were duly and swiftly implemented to the overall satisfaction of FATF, Council of Europe and EU. Analysing how the financial sector developed in Latvia following the adoption of FATF institutions can thus highlight the 'FATF effect' on illicit finance.

Given the potential importance of FATF to reducing the offshore finance-corruption nexus, this research question falls under one of the Economic and Social Research Council's (ESRC) five research priorities for 2016-2020: namely critical, innovative research on banking that goes beyond "mainstream academic macroeconomics," given the "limited relevance of mainstream macroeconomic theory to associated policy debates" (RCUK 2016 p15).

1.2 My argument in brief: Latvia, the 'onshore offshore' financial centre

Defining an offshore financial centre (OFC) by financial data as *"a country or jurisdiction that provides financial services to nonresidents on a scale that is incommensurate with the size and the financing of its domestic economy"* qualifies Latvia as an OFC hosting "numerous offshore banks and companies serving mainly non-resident CIS clients, with offshore investment coming from Eastern Europe and Russia" (Zoromé 2007 p7, p17). Latvia's offshore banking sector handled sizeable dollar funds for non-resident shell firms with hidden ownership, until US Treasury intervention forced it to close in 2018.

However, beyond the financial data, Latvia had none of the usual regulatory identifiers of an OFC such as low tax rates and high levels of corporate secrecy provided to non-residents. What then attracted non-resident money to Latvia? My argument is that, firstly, Latvia starting even before independence from the Soviet Union radically deregulated its banking sector, opening it up to shell firms domiciled in secrecy jurisdictions and holding dollar deposits. It did so as part of a laissez-faire, monetarist financial policy pursued in the Soviet aftermath. Secondly, the lack of formal characteristics of an OFC and early legislation of the FATF rules meant that Latvia was 'whitelisted' by FATF and other international bodies, which lent legitimacy to money of dubious origins routed via Riga. Thirdly, there was a practice of informal ringfencing of Latvia's non-resident sector from the enforcement of AML laws, which was the core of Latvia's competitiveness as an OFC. Although informal in nature, this can be equated to the regulatory ringfencing typical of an offshore, creating a space of exemption for non-residents from onshore constraints. The combination of these three factors meant that Latvia was an 'onshore' OFC: the local bank sector was formally onshore, and well-regarded, but de facto offshore. The main financial operation performed by the offshore sector was routing dollar payments between the former Soviet states and the global financial system.

Thus, the answer to the question of the impact of FATF on illicit offshore finance in the case of Latvia is troubling. Latvia's significance as an OFC was that it was not one - according to formal regulatory criteria. Latvia indeed won praise for its AML laws and overall good governance, enjoying an excellent international reputation. In many ways, Latvia was a model pupil of FATF. Precisely this, I argue, enabled it to act as an OFC for the shadow economy of the CIS states, i.e. effectively as a money-laundering hub. In the 1990s, Latvia was implicated in post-Soviet flows of illicit offshore dollars. However, Latvia was an early adopter of AML, while other post-Soviet countries such as Russia and Ukraine were both blacklisted after 2000. Nevertheless, Latvia's impressive implementation of AML and overall 'good governance' credentials did not result in a decline in the flow of offshore dollars from the CIS via Riga. On the contrary, the implementation of AML was accompanied by a sharp rise in dollar flows such that it has been estimated that after 2010, 1% of global dollar transactions cleared by US correspondent banks were being booked via Latvia (Bloomberg 2018, Jemberga and Purina 2016). These were largely dubious funds of unclear origins linked to the post-Soviet shadow economy. Even before the US Treasury intervention of 2018 forced the closure of offshore banking in Riga, it was clear that Latvia had become a fully-fledged money-laundering hub for the CIS countries, dubbed belatedly as the "Bond villain of the world economy" (Sommers 2018).

The FATF regime expanded fast across the world because it 'named and shamed' on blacklists and greylists whole countries failing to comply with its requirements, thereby leveraging the power of reputation and legitimacy rather than diplomacy to influence countries into adopting AML (Sharman 2011). But money laundering is the feigning of financial legitimacy, and therefore incorporates reputation and status factors into its calculations when structuring dirty money. The FATF-inspired proliferation of indices of financial legitimacy is thus grist to the money launderers' mill. In particular, FATF's geographic normativity - the labelling of whole countries as compliant or non-compliant with AML requirements - successfully pressured countries to comply with its standards to avoid blacklisting but created a geography of financial legitimacy that money launderers reference to legitimise undeclared funds.

1.3 Setting the scene: Riga as a banking centre

In the early 1990s, Riga's historic centre, with its medieval Hanseatic old town and Art Nouveau new town, looked the part of a potential European banking centre as it emerged from the Soviet gloom. The fledgling private banking sector saw Riga's architectural legacy and pre-war banking history as a source of legitimacy. In 1994, the Association of Latvian Commercial Banks (ALCB) published a lavishly illustrated history of Riga banking "then and now" to underscore Riga's past as a financial centre during the late Russian Empire as a foundation to build a new financial centre upon (Zalite 1994). Latvia's post-Soviet bankers seized on this heritage, despite no institutional continuity surviving the decades of Soviet rule. They named their new banks after famous banks from the 'golden age' and headquartered them in historic buildings. The autobiography of Latvia's most famous banker, billionaire Valērijs Kargins, starts with a chapter not on his childhood, but one entitled "A history lesson" about Riga's pre-Soviet banking tradition (Kargins 2005).

Riga's 'golden age' as a commercial centre in the Russian Empire in the second half of the nineteenth century and early twentieth century had seen Riga's population expand from around 60,000 in 1860 to 472,000 by 1913, becoming Russia's fifth largest city, accounting for around 5% of the Russian empire's GDP (Hein-Kirchner and Misāns 2016, Eglitis 2017). The city's ethnic composition also changed from majority German-speaking to Latvian-speaking because of rural-urban migration. Riga's population more than doubled again during Soviet industrialisation after the Second World War to reach 900,000 by 1989 (Hein-Kirchner and Misāns 2016, Lieven 1994). Ethnic composition changed in this process too: this time the migrants were Russians and other Soviet nationalities, so that by 1990, as much as 50% of Riga's population were Russian speaking (Auers 2015).

The history of Riga stretches back to the city's founding in 1201 by the crusading Teutonic Knights and its subsequent membership of the Hanseatic League of merchant cities in the Middle Ages. The history of the Latvian state is considerably shorter. Latvians' national awakening emerged at the end of the nineteenth century, but independence came largely fortuitously in the First World War, as the result of the collapse first of the Russian Empire, then of Imperial Germany. Latvia tragically lost its independence again in 1939 as the two successor empires, the Third Reich, and the Soviet Union, first cooperated then clashed. As a result, the Soviet Union incorporated Latvia as one of its Union Republics. A Latvian independence movement gathered pace during Soviet General Secretary Mikhail Gorbachev's reform policies of *Glasnost* and *Perestroika* in the second half of the 1980s. After a failed putsch by Soviet hardliners in August 1991 sealed the breakup of the Soviet Union and Latvia's independence, Latvia's national movement restored the parliamentary constitution of 1922. The restoration also restricted Latvian citizenship to descendants of the pre-war citizenry, thus initially disenfranchising much of the Russian-speaking population. In 1995, Latvia and its neighbours Estonia and Lithuania were put on the path for future membership of NATO and EU, joining in 2004. Latvia then joined the Eurozone in 2014 and OECD in 2016. Despite these apparent successes, Latvia's population decreased by nearly a third from 2.7mn in 1989 to 1.9mn in 2019 (CSBL 2020).

The capital Riga now comprises one third of the population of Latvia. In this thesis, I will use 'Riga' and 'Latvia' interchangeably when referring to the site of the offshore banking hub, and 'Latvia' when referring to aspects of the jurisdiction.

1.4 Structure of dissertation

In the second chapter, I provide an overview of research on offshore finance and its centralities in economic geography and the social sciences. I identify two waves of research: the first wave comprising largely qualitative case studies of tax havens dating from the mid-1990s, the second largely quantitative wave of research on global networks of offshore investment. The third chapter surveys critical literature in the governmentality tradition on the regimes put in place to regulate offshore finance and combat money laundering and funding of terrorism, under the aegis of FATF. This chapter introduces blacklisting, greylisting and whitelisting as key technologies mobilised in the FATF regime, and prepares the theoretical framework for the results chapters, in particular Chapter 6 and Chapter 8.

The fourth chapter on research design and methodology addresses how I propose to tackle the research question: the effect of the FATF regime on the geography of illicit offshore finance in the case of Latvia. Latvia is a suitable case study to address this question because it is the only financial centre to have transitioned from the ruins of the Soviet Union and financial chaos of the 1990s to membership of EU, NATO, Eurozone and OECD, while implementing FATF requirements. I describe a dual methodology comprising of semi-structured interviews on the one hand and digital data on the other, discussing the nuances and ethical issues arising from both research strategies.

In the fifth chapter, the first of four results chapters, I discuss the role commercial banks played in the collapse of the Soviet Union. Then I describe the rapid expansion of US dollar correspondent banks across the post-Soviet space in the 1990s and their engagement with the myriad new local commercial banks. With reference to the literature on offshore financial centres, I discuss this process in more detail in Latvia, despite its newfound independence still strongly involved in the post-Soviet financial network. In the sixth chapter, with reference to the theoretical discussion in Chapter 3 of governmentality and its technology of lists, I discuss how Latvia was effectively whitelisted after 2000 on implementing the FATF requirements. Well-regarded Scandinavian banks dominated Latvia's domestic retail banking sector while Latvia's offshore banking sector, a legacy from the 1990s, lobbied the US to retain unfettered access to dollar correspondent accounts. Parallel to Latvia's achieving high AML standards on paper, the flow of post-Soviet dollars through Latvia's offshore banks soared.

In the seventh chapter, I examine the shadow-economy operations of the Riga offshore banks by focusing on their shell firm clients. I use a web scraper, analyse leaked bank transactions, and mine Ukraine's online court decisions database, to conclude that Latvia as an offshore financial centre was specialised in shadow economy operations until 2018, i.e. acted as a money laundering hub, benefiting thereby from its whitelisted status and high FATF rankings. In Chapter 8, I chart attempts by a number of governments to deal with Riga's offshore banking sector and its money laundering activities, at the same as they were to varying degrees themselves implicated in its activity. I argue that it was not the governmentality of the FATF regime as analysed in Chapter 3, but US authorities acting in pursuit of US sovereign interests that finally closed down Latvia's offshore sector in 2018. In the conclusion I look back on the history of Riga's offshore banking sector 1992-2018 to answer how FATF may impact on illicit offshore finance, and the implications for our understanding of financial capitalism.

Chapter 2. Offshore Financial Centres in the mirror of Economic Geography

2.1 Introduction: Defining OFCs

Shortly I will review the financial geography literature on offshore financial centres (OFC), but first I will address problems surrounding the term. As scholars have pointed out, major offshore financial hubs such as UK are not generally referred to as OFCs, whereas some jurisdictions labelled OFC lack a financial sector altogether (Zoromé 2007, Shaxson 2011, Sharman 2011 Binder 2019). The lack of clarity about what constitutes an OFC can be explained through the term's emergence. It originated as the self-designation of the jurisdictions commonly labelled 'tax havens' in the course of the 1980s as they became more conscious of reputation. The tax havens introduced OFC as a neutral self-designation to avoid the stigmatisation associated with 'tax haven,' which foregrounds tax and its diversion from onshore jurisdictions (Hampton 1996). The term OFC was then tentatively adopted by some international organisations at the turn of the 21st century as attempts to regulate OFCs gathered pace (FSF 1999).

A division then emerged between international organisations involved in macroeconomic regulation and those involved in tax regulation. The former, primarily the IMF, used the term 'OFC', which they defined not by legal provisions, but quantitatively, by measuring the ratio of financial services provided to non-residents against the size of the domestic financial sector. This definition includes, for instance, the UK as an OFC, thus expanding the OFC notion from 'tax haven' to include a major global financial centre (Zoromé 2007). The OECD on the other hand, uses the terms 'tax haven' and 'OFC' interchangeably to denote jurisdictions with regulation harmful to onshore tax regimes (OECD 1998).

As we shall see during this chapter, social scientists have also alternated between defining OFCs by financial data or regulatory provisions. They have additionally thematised the importance of reputation to OFCs noted above. In the first part of this chapter, I outline the 'first wave' of social science research into offshore finance and its centralities prior to the global financial crisis of 2007-9. I then outline a 'second wave' of research that followed the crisis. At the end of this chapter, I will discuss the range of definitions provided by scholars more fully.

2.2 First research wave: Offshore finance between global cities and tax havens

The end of the Cold War saw the adoption by most post-socialist states of neoliberal policies already orthodoxy in the West, including trade and capital account liberalisation. Together with China's capitalist turn, and new telecommunications technology, the world economy was more integrated than ever before. Social scientists' attention swivelled from the east vs west confrontation to globalisation.

Two scholars provided contrasting frameworks for researching globalisation at the start of the 1990s. One was Marxist geographer David Harvey's theory of the 'spatial fix' to capitalist crises, which treated globalisation as the latest manifestation of capitalism's drive towards temporal and spatial expansion to alleviate its internal contradictions (Harvey 1982). The second was liberal political economist Susan Strange's writings on financial globalisation, termed "casino capitalism" to denote the reshaping of global governance by the power of financial markets (Strange 1986). Both Harvey and Strange made crucial contributions to their respective disciplines: critical geography and international political economy. The tension between the critical approach (Harvey) and the liberal approach (Strange) has remained at the core of scholarly debate regarding financial globalisation.

Urban sociologist Saskia Sassen then drew on both approaches to identify the clustering of advanced business services (ABS) in major world metropoles as comprising 'a global city' (Sassen 1990). These expert innovative services in finance, law, accounting, and advertising operate worldwide in the service of transnational business: "It is clear that we are dealing with a cross-border system, one that is embedded in a series of cities (…) It is a de-facto global system" (Sassen 1990 p352). Sassen's hypothesis was that as economic activities become globally dispersed, central corporate functions become both more important and more specialised. Because these central functions are so specialised, especially in finance, transnational firms outsource them to ABS. ABS are subject to agglomeration economies because they must intensively interact with each other to provide coordination functions to transnationals. They also provide their services transnationally, meaning that global cities form a cross-border urban network detached from the hinterlands of the cities (Sassen 1990).

In parallel to Sassen, British economic geographers also pivoted to the study of financial geography at the start of the 1990s in the face of accelerating globalisation. As Nigel Thrift argued, "I simply cannot understand why so little attention is paid to matters of money and finance in human geography: it is a genuine mystery to me" (1990, p1135). This was the announcement of a new research agenda examining the geography of financial centres, which led to Thrift and Leyshon publishing a study of London as a financial centre. Due to its 'offshore' role as centre for the Eurodollar market, the City of London had "changed quite decisively in ways which are intimately linked to its transformation into an outpost of an electronic phantom state" (Leyshon and Thrift 1997 p307). The new research agenda repudiated a provocative new thesis that telecoms and information technologies had rendered geography irrelevant to finance. O'Brien's book *Global financial integration: the end of geography* (1992) argued that new technologies caused "all the geographical terms become harder to define and at the extreme become meaningless" (O'Brien 1992 p4). In chorus with Sassen, Leyshon and Thrift argued the opposite, that the financial service industry was highly concentrated in a handful of global locations such as the city of London. "Post-Bretton Woods (…) the number of these international financial centres that count (…) has decreased but, in turn, those places that are left in contention have become more important (…) These are the places that make the non-place electronic realm conceivable" (Leyshon and Thrift 1997 p307).

Ronen Palan added the study of offshore finance to that of globalisation and its financial centres. Palan traced the metaphorical usage of the term back to the 'offshore' radio broadcasters of the 1950s and 1960s, such as Radio Caroline, which broadcast US pop music 'offshore' from a foreign registered ship docked in the Thames (Palan 2003). Broadcasting, like finance, was at the time tightly regulated, while having the inherent capacity to break free of national boundaries. This indicated that "the presumption of strict territorial sovereign boundaries may be a necessary fiction, but cannot be sustained in reality" (Palan 2003 p36). As the Euromarket in US dollars developed in London in the 1960s, in an analogy to Radio Caroline's US pop music, the term 'offshore' came to apply to it (Palan 2003).

Palan follows Leyshon and Thrift, Strange and Sassen in identifying the birth of offshore finance not in tax havens, but in the growth of the Eurodollar market in London, resulting from a decision of the Bank of England in 1957 not to regulate transactions performed in the UK between non-residents in foreign currency. The decision placed such transactions outside of UK regulations, while they were also absent from other states' regulation (Palan 2003). The effects of this new Euromarket rippled out across the globe, according to Palan, as existing tax havens attracted it, which in turn stimulated the creation of new ones used as booking jurisdictions (Palan 2003). Besides the small island jurisdictions, Palan also examines the European ‘anachronistic’ states of Switzerland, Luxembourg, Liechtenstein, Monaco, Andorra and Gibraltar, often neglected by geographers of global and offshore financial centres. Largely because of their size, these statelets had failed to develop the national taxation frameworks adopted by their industrialised neighbours in the 20th century, while already possessing strong legal institutions and banking secrecy, turning them into tax havens by default (Palan 2003). Palan et al went to identify seven major types of OFCS classed according to function, ranging from the South Pacific island of Vanuatu to London and New York.

Table 1. Typology of offshore financial centres

Name	Role	Example
Incorporation locations	the registration of offshore companies used in transactions recorded in other tax havens, lack a banking centre.	Montserrat and Anguilla
Registration centers	reinvestment of money in its country of origin, i.e. “round tripping, some local financial expertise	Panama for the U.S. market, Jersey for London, Vanuatu for Australian market
Secrecy locations	secrecy is paramount and heavily protected	Liechtenstein, the Turks and Caicos Islands, Singapore, and Dubai
Specialist service providers	provide a specific type of business activity.	Bermuda and Guernsey for the reinsurance market, the Caymans the hedge fund industry, the Isle of Man UK’s Alternative Investment Market
Market entry conduits.	earn a margin from the routing of transactions, exploiting a network of double tax treaties	Malta and Cyprus for EU, Mauritius for India, Netherlands for EU
High net worth providers	manage funds deposited by the world’s wealthiest people	Switzerland, New York, and London
Tax raiders	seek the relocation of profits, by taxing them at a lower rate and offering financial security while not widely regarded as tax haven	Ireland

Source: (adapted from Palan et al 2013 p37-38)

Case studies of tax havens

In parallel to these works, several case studies of individual tax havens examined the relationship between the tax haven as a jurisdiction, the financial flows, the onshore jurisdictions where the financial flows originate, and other tax havens. The main structural change driving the emergence of new tax havens was the growth surge in the Eurocurrency markets in the 1970s driven by the recycling of petrodollars resulting from the OPEC oil price shock (Roberts 1995). This growth in offshore dollar banking caused international banks, mostly from the US, to look for low tax locations with suitable legal and linguistic infrastructure. This powered the spread of tax havens as if offshore finance was "secreting distinct new spatial forms" (Roberts 1995 p252):

> a series of new financial centers (…) came to account for a significant portion of the world's cross-border bank claims appeared on the world map. From the Bahamas to Luxembourg to Vanuatu, small and often marginal places became offshore financial centers (OFCs): new and distinctive spaces corresponding to nodes in the circuits of offshore financial markets that developed in the 1970s. (Roberts 1995 p238)

Roberts and – separately – another geographer, Alan Hudson, focused on the Cayman Islands, a tiny British colony in the Caribbean with population of just 58,000 that became the offshore hub of the global hedge fund industry. Under guidance of US bankers, Cayman had established appropriate legislative framework and a zero-tax regime. As a result, hundreds of international banks set up a presence in Cayman, mostly as a legal fiction: of the over 500 banks registered there in the early 1990s, more than 80% had no physical presence on the island except a 'brass plate'. By 1992, Cayman banks held $400bn in external assets (Roberts 1995, Hudson 1996).

Roberts and Hudson use the term 'offshore financial centre' rather than tax haven to describe Cayman. However, they both make it clear that Cayman and competitors such as Bahamas were mere booking centres, rather than banking centres in their own right: "The Eurocurrencies that are 'booked' to Cayman shell branches do not actually come to the Islands but are merely entered into a ledger or a computer file by the parent bank's staff onshore" (Roberts 1995 p244). Even where a foreign bank opened an office as opposed to a mere ‘brass plate’, it performed only bookkeeping functions. As one banker in the Bahamas told Hudson:

> Offshore banking means that there are no funds in the Bahamas. All the funds we manage are abroad, not in the Bahamas. So for clients there is no Bahamas country risk. It’s an offshore country risk, a Swiss risk if it is a Swiss bank (…) If the Bahamas, politically, goes under, the only risk is that we, the bank’s furniture and people and building, are at risk. No money is at risk. Book-keeping wise we have double accounting. If we are destroyed by a hurricane we can work tomorrow, normally. There’s nothing lost (Hudson 1996 p105)

Roberts and Hudson also drew on the concept of competition between places to describe how Cayman competes with other offshore centres (Amin and Thrift 1993). Indeed, according to Roberts, "competition is the condition of existence of all financial centers" (Roberts 1995 p250). Thereby places act ‘entrepreneurially’ in concert with advanced business services to position themselves in offshore financial flows. According to Hudson, the specific importance of ‘place’ to OFCs is the creation of a competitive local regulatory framework and thus “place matters in offshore finance because regulation matters and regulation is geographical” (Hudson 1996 p107). In the case of Cayman, according to Hudson, the offshore legislation was copied from the Bahamas, a competing OFC, and comprised laws enshrining the twin essentials of maximum secrecy laws and zero tax. But Cayman overtook Bahamas when Bahamas declared independence from UK, since the move prompted instability and rumours relating to the Bahamas’ leadership’s ties to drug money laundering (Hudson 1996).

This underlines that reputation had become very important to an OFC alongside zero taxation and secrecy. Cayman being a colony of the UK helped it outcompete other jurisdictions in this regard (Hudson 2000). Cayman coined the slogan 'Reputation is our most important asset’, which many tax havens then adopted in numerous different permutations (Hudson 1998 p928, Sharman 2006). ‘Reputation’ was the word most used by respondents to explain success or failure of tax havens (Hudson 1998). Sensitivity to reputation was such that Cayman Islands officially repudiated a fictional portrayal of Cayman money laundering by a bestselling US fiction author (Sharman 2006).

Hudson and Roberts note that Cayman's concern about reputation left little tolerance for either external criticism or internal dissent, adding to oligarchic backroom politics typical of OFCs. Mark Hampton and John Christensen's study of Jersey argues that the development of OFCs results from capture of the local jurisdiction by financial capital. Small island states are easy prey for international finance because their political structures are inherently oligarchic (Hampton 1994, Hampton and Christensen 2002). Hampton and Christens describe how the 'Big 5' international accounting firms successfully lobbied Jersey to legislate for limited liability partnerships similar to those in the state of Delaware, USA (Hampton and Christensen 2002). According to Hampton, once financial capital commandeers an offshore jurisdiction, the offshore financial sector crowds out other sectors, even tourism, creating a feedback loop to state capture (Hampton and Christensen 2002).

Susan Cobb's analysis of the Isle of Mann as an offshore financial centre (Cobb 1998) draws strongly on Amin and Thrift's work on "holding down the global" and "competition between places" (Amin and Thrift 1993). Like Hudson, Cobb emphasises that success in the competition among offshore jurisdictions requires the maintenance of a 'good reputation' based on efficient regulatory institutions and a local knowledge base, i.e. well-trained staff (Cobb 1998). Cobb thus sees reputation as crucial, but more as a rational reflection of good regulation, rather than the results of concerted PR.

> The location of an OFC, its political relationship with the nearest onshore jurisdiction and concomitant level of political stability are long-term fixed characteristics of the place. What can be, and is, changed through the actions of local actors and local global networks is the reputation of the place and its subsequent success in the amount of capital attracted to that place. (Cobb p165)

Cobb uses the Isle of Mann to present a more liberal view of OFCs. If OFCs add value to transactions, they are not purely tax havens, she argues. Instead of 'state capture' by global financial services, as Hampton and Christensen argued was the case in Jersey, Cobb talks of the Isle of Mann receiving a "sophisticated regulatory massage" from financial services leading to similar legislation as in Jersey (Cobb 1998 p17).

In contrast to the Caribbean booking centres detailed above, Barney Warf's study of the Panama offshore banking sector highlights that Panama comprises a large 'real' banking sector that initially developed to serve the canal shipping (Warf 2002). Panama was fully dollarized, with no taxation of business owned by foreign citizens. In the early 70s Panama deregulated its banking sector while increasing banking secrecy. The result was “a bona fide commercial centre that has become the nation's largest single source of employment and foreign revenues,” which is also the “largest and arguably most important international financial centre in Latin America” (Warf 2002 p36). The flood of petrodollars into offshore finance prompted international banks, mostly US, to open Panamanian subsidiaries for clientele across Latin America. Besides shipping, dollarization and deregulation, a fourth factor supporting offshore banking was Panama’s advanced corporate telecommunications network, a legacy of the US military presence in Panama. Panama also provides corporate secrecy for non-residents. “The use of shell companies, including holding corporations and, increasingly, foundations, blurs legal lines of liability (…) protecting assets (both legal and otherwise) from public scrutiny through deliberately impenetrable webs of cross-ownership that typically deflect even the most dogged of auditors” (Warf 2002 p43).

What is a shell firm? While any company is a ‘legal person’ that can own assets, enter contracts and be taken to courts, most companies are much more than this, having a physical presence in the form of employees, offices and warehouses, and an economic substance in the form of a business selling products or services. Shell companies however comprise only the legal personality, without physical presence or economic substance, hence the term (Sharman 2011). Shell firms can be finely tuned constructs used as ‘special purpose vehicles’ in structured finance (see below) or a piece of paper issued by a Caribbean island that keeps no corporate records itself. In the latter case, shell firms are notorious for facilitating money laundering because their structure creates anonymity for owners, while the entity is also ultimately disposable, since it does not own assets. “The defining metaphor is of shell companies functioning as a corporate veil: screening and separating criminals from illicit financial activities (Sharman 2011 p125). Like the Bahamas as discussed by Hudson, Panama’s reputation suffered greatly from allegations that it launders narcodollars via its shell firms and banks, allegations that local bankers attribute to a smear campaign by competing OFCs (Warf 2002). While shell firms conceal their owners, they can rarely hide to investigators the jurisdiction where they are registered, and thus through successfully protecting criminals, they damage the reputation of their domicile.

Political scientist Jason Sharman drew on these and other studies’ findings to argue for ‘reputation’ as being a key resource for OFCs.

> The success or failure of a tax haven is more dependent on its reputation than any other single factor. (…) [R]eputation is the main point of differentiation among a relatively large number of tax havens that are engaged in fierce competition with each other within and across regions (Sharman 2006 p107)

Sharman argued that tax havens "obsessively" protect their image. "The comment that 'perception is more important than reality' is a constant refrain in interviewing those from the public and private sector involved in offshore finance (…) Reputation is the main asset of a tax haven but also its main vulnerability" (Sharman 2006 p114). The very term 'offshore financial centre' derives, as stated earlier, from moves by tax havens to improve their reputation by introducing a euphemistic self-designation (Sharman 2006). The consequences of bad reputation could be very real. In comparison to the British colony Cayman, the reputations of both Bahamas and Panama, being independent, suffered from the behaviour of their respective political leaderships, Lynden Pindling in the Bahamas and Manuel Noriega in Panama (Hudson 1996, Warf 2002). In December 1989, the US then invaded Panama claiming extensive drug money laundering.

One point of criticism of these case studies in the 'first wave' of research into OFCs is the "conflation of offshore finance with so-called tax havens," which has "tended to focus the research on specific jurisdictions linked in a wider process, rather than placing primacy on the processual aspects of the offshore" (Maurer 2008 p157). As noted above, many tax havens had little home-grown banking that could see them qualify as genuine financial centres. Moreover, the lack of data available on offshore financial flows at the time made fieldwork onsite in tax havens one of the few viable access points for research into offshore finance. In the next section we will see how this changed.

2.3 Second research wave: Mapping offshore finance

Despite the importance of the above research, concerns grew after the turn of the century that economic geography was failing to fully tackle financial globalisation. "The syndrome of processes currently bundled together within the term 'globalization' is intrinsically geographical, as are the outcomes of such processes. Yet, once again, it seems, we are not, as a discipline, centrally involved in what are clearly very 'big issues' indeed" (Dicken 2004 p5). Thus, when the credit crunch struck in 2007-2009, there was a sense of urgency among economic geographers that the discipline should take its rightful place, rather than again ‘miss the boat’ (Engelen and Faulconbridge 2009 p588).

One way for geographers to contribute was by focusing on OFCs’ role in the crisis. Economic geographers argued that the crisis had originated within international financial centres, via the competition between global financial centres to create new investment instruments while deregulating (French et al 2009). This prompted new attention by geographers to offshore finance (Wojcik 2009).

> [It is the] responsibility of economic geographers to remind the world of the significance of financial centres as concentrations of financial activity, expertise, and power (…) The ABS-offshore nexus is central to the discussion on the reform of the global economic governance (Wojcik 2013 p15).

At the same time, new data-led approaches to offshore finance became viable, as international financial institutions, in particular the Bank of International Settlements (BIS) and IMF, expanded their data offerings (Coates and Rafferty 2007, McGuire and von Peter 2009). An additional boon have been new data sets provided by Switzerland and Luxembourg providing monthly banking data covering all wealth in all banks operating, including branches of foreign banks. “No other country in the world produces anything similar” (Zucman 2015 p28). Such data-driven mapping of the global network of offshore flows has drawn respectively on databases for: foreign direct investment (Haberly and Wojcik 2015a, 2015b); foreign portfolio investment (Coates and Rafferty 2007, Zoromé 2007); BIS banking statistics (Fichtner 2014); regulation and taxation (Cobham et al. 2015); private wealth (Zucman 2015); corporate ownership networks (Garcia-Bernardo et al. 2017) and stocks and flows of corporate financialization for multinationals, investment funds and banks (Fernandez and Hendrikse 2020).

A special edition of Economic Geography in 2015 echoed Palan’s 2003 work in tracing the genealogy of the term ‘offshore finance’ (Cobham et al 2015, Palan 2003, Maurer 2008). The authors argue that the term has value mostly because of the established research tradition in economic geography (Cobham et al 2015). They define OFC as “any jurisdiction through which financial claims pass to avoid policy constraints elsewhere” and offshore finance as “the activity of using such jurisdictions or, put differently, the activity of booking and/or registering financial claims in a jurisdiction to avoid policy constraints in other jurisdictions”

(Cobham et al 2015 p241). This definition avoids prejudging offshore finance: it allows for attempts by emerging economy actors to access independent and efficient institutions in an OFC, such as courts, that are unavailable domestically. It also allows for different degrees of offshoreness, depending on the mixture of motivation.

Haberly and Wojcik used the IMF and BIS datasets to create the first comprehensive map of the interrelationship between OFCs, operationalising offshore investment as foreign direct investment (FDI) that is disproportionately large compared to the interacting economies. They find the main sources of offshore FDI globally are the British Virgin Islands, Luxembourg, the Cayman Islands, the Netherlands, Switzerland and the UK (Haberly and Wojcik 2015). The driving force behind the implementation of offshore finance are not the offshore jurisdictions, but advanced business service sector firms headquartered in the global cities which design most of the financial sector legislation enacted by offshore jurisdictions (Wojcik 2011). Thus, according to Wojcik, the best place to research offshore finance is not the Caribbean, but New York and London (Wojcik 2011). The New York - London axis' commonalities in language, law and free market culture and the time zone complementarity supported by intensive infrastructure networking creates a near seamless continuum (Wojcik 2011 p2). London's position as the apex of a 'offshore archipelago' or 'second empire' of British current and former colonies with a common law legal framework is unchallengeable, rather than being vulnerable to competitive deregulation from other jurisdictions (Haberly and Wojcik 2013). The same applies to the role of the dollar in offshore finance, and therefore the extension of an aspect of US sovereignty, the 'dollar umbrella' (Haberly and Wojcik 2013). Haberly and Wojcik argue that the 'supply side' of offshore finance - the established system as it exists today having developed historically as a legacy of empires and power blocs - is determining. The ABS-offshore nexus is 'sticky', a "deeply rooted product of the interaction of global capitalism with the sovereign state" which "should be understood with reference to a timescale of centuries as opposed to an individual business day" (Haberly et al 2015 p255, Haberly and Wojcik 2013 p253). This means that it could be regulated if there were political capacities to overcome the entrenched interests.

While ABS are centred in New York and London, the investment vehicles they design and manage for clients are registered across a range of jurisdictions, depending on their function and the combination of tax advantages and secrecy they require. Holding companies are incorporated in the Netherlands, Belgium and Switzerland, trusts are domiciled in Jersey, hedge funds and special purpose vehicles (SPV) on the Cayman Islands, collective investment funds in Luxembourg (Wojcik 2013). This is what creates the map of FDI described above. On a lower level than ABS are company service providers based in London or New York, who do the more mundane work of administering SPVs across diverse jurisdictions, organising nominee directors and ensuring tax neutrality (Wainright 2017). 30-50% of FDI worldwide is tax-related, implemented via investment vehicles (shell companies, SPVs) in tax havens (Haberly and Wojcik 2013). The use of shell companies domiciled in offshore zones decouples the jurisdiction of registration from the ownership of the assets, allowing tax minimisation or evasion supported by secrecy of ownership.

Another notable effort to map global offshore finance is the Corpnet project at University of Amsterdam. The project mined the Orbis corporate database to analyse investment flows between nearly 100 million firms worldwide and 71 million corporate ownership relations (since not all firms have corporate subsidiaries or parents) (Garcia-Bernardo et al 2017). Based on their analysis, the authors distinguished between ‘sink OFCs’ and ‘conduit OFCs’. Sink OFCs retain foreign investment flows, while Conduit OFCs route investment internationally without taxing it, allowing profits in one country to be re-invested in another. The authors identified 24 Sink OFCs, of which the five largest were Luxembourg, Hong Kong, BVI, Bermuda and Jersey, while five countries acting as the main conduits for global investment flows: Ireland, Singapore, the Netherlands, the UK, and Switzerland. However, since the Orbis database does not contain data on many secrecy jurisdictions, as the authors acknowledge, the results understate the role of some classic tax havens. The role played by highly developed countries such as Ireland, Singapore, the Netherlands, the UK, and Switzerland as OFCs contrasts with the standard image of OFCs as “exotic small islands that cannot be regulated”, for “[o]nly a small set of territories act as sinks of ownership chains (most of them under British sovereignty), and even a smaller subset act as conduits for ownership structures to sinks” (Garcia-Bernardo et al 2017 p9).

‘Elsewhere, ideally nowhere’: From analysis to advocacy

In contrast to this descriptive-historical approach tracing the presence of offshore investment flows, critical approaches by advocates of tax reform such as Tax Justice Network (TJN) and their academic allies analyse offshore finance as an absence: namely the absence of tax revenues from onshore economies, which they term “one of the most important political issues of our times" (Palan et al 2010 p13). Offshore finance is "[e]lsewhere, ideally nowhere" (Palan and Nesvetailova 2014). By analysing offshore finance in this way as an ongoing absence of tax revenues from onshore economies, Palan et al emphasise that tax havens are not "on the margins of the world economy, but are an integral part of modern business practice" and that offshore finance is quotidian (Palan et al 2010 p4):

> the run-of-the-mill employee of an international corporate, financial or consulting firm is likely to encounter offshore finance as a daily reality of their lives. Companies that are not taking advantage of the offshore world are viewed as odd anomalies, or as even reneging on their commitments to shareholder value (Palan 2012 p300).

The role of tax havens is thus expressed as a negative: "in one word - avoidance (…) the abstract expression of the collective efforts of the state, corporate, and business elites of the world to avoid the very laws and regulations that they have collectively designed" (Palan et al 2010 p6). Tax avoidance undermines the sustainability of wealth creation in the onshore economies and shifts the gains from globalisation to the select few who access this offshore space. Palan et al argue that tax havens are less a geographical phenomenon than a legal fiction within the onshore economies enabling tax avoidance (Palan et al 2010).

Tax campaigner Richard Murphy puts not a location but a legal property - secrecy - at the heart of offshore finance (Murphy 2009) and proposes substituting 'secrecy jurisdiction' for 'tax haven.' Without the veil of secrecy that such jurisdictions provide to economic transactions taking place elsewhere, their tax regulation would not be effective. Murphy argues that:

> the assumption that the secrecy world is geographically located is not correct. It is instead a space that has no specific location. This space is created by tax haven legislation that assumes that the entities registered in such places are 'elsewhere' for operational purposes, i.e. they do not trade within the domain of the tax haven, and no information is sought about where trade actually occurs (Murphy 2009 p2).

Murphy and collaborators differentiate between tax havens as booking jurisdictions, i.e. a legal fiction, and 'real' offshore banking centres. Arguing that many 'offshore' banking centres are not offshore, and one, Liechtenstein, is even doubly landlocked, they relabel the offshore finance as the 'secrecy space'. For example, a UK resident not domiciled in the UK establishes a trust in the British Virgin Islands that in turn owns a firm incorporated in Jersey that in turn has nominee directors from Cayman and a bank account in the Isle of Man (Murphy 2009). This structure, albeit expensive, is almost entirely unregulated, therefore effectively ‘nowhere’, i.e. in the secrecy space, according to Murphy

Seabrooke and Wigan’s work on Global Wealth Chains likewise highlight how it is by combining the advantages of different OFCs that capitalists succeed in minimising their onshore footprint. Global Wealth Chains are defined as “transacted forms of capital operating multi-jurisdictionally for the purposes of wealth creation and protection,” and also described as “linked forms of capital seeking to avoid accountability during processes of pecuniary wealth creation” (Seabrooke et al 2017 p2). The most notorious Global Wealth Chain is the so-called ‘Double Dutch sandwich’: a special purpose vehicle owning intellectual property rights in Bermuda realising royalties from sales by Dutch and Irish subsidiaries of the US company. Such a construction implies “the disaggregation of asset ownership, costs and revenues across multiple countries” (Bryan et al 2017 p94).

Typical of critical approaches to offshore finance is the suspicion that much of it is illicit: proceeds of crime, bribery and corruption, illegal capital flight, tax evasion (Murphy 2009). “It is a space where legitimate business turns to criminal behaviour - using offshore facilities for tax evasion purposes - while criminal businesses use offshore facilities to go legit” (Palan 2009 p35). Raymond Baker, co-founder of another NGO Global Financial Integrity, another collaborator in the tax reform advocacy group, estimates total illicit flows at between $1 trillion and US$1.6 trillion a year, of which around two thirds is tax evasion (Baker 2005, Sikka 2004). Tax Justice Network analysts established the Financial Secrecy Index (FSI), a ranking that combines jurisdictions’ extraterritorial financial weight with their respective level of secrecy (Cobham et al 2015). Jurisdictions with high levels of extraterritorial financial impact combined with high levels of secrecy correspond to the classic definition of a tax haven (Cobham et al 2015). The Financial Secrecy Index (FSI) shows “a spectrum of secrecy rather than a binary distinction between tax havens and others” (Cobham et al 2015 p297). The term also includes the United States and the United Kingdom, incorporating the “realization that offshore is a pervasive aspect of the world economy, rather than a group of troublesome (small) jurisdictions” (Cobham et al 2015 p286). By this move, argue the authors, the concept of tax havens ceases to be discriminatory, and any political battle with offshores loses its post-colonial power dynamics.

Tax Justice Network calculated that a total of $21 trillion is held offshore by triangulating three independent methodologies, extensive statistical analysis as well as interviews with bankers, lawyers, and other offshore experts (Henry 2012). The core of the methodology was to total cross-border deposits as calculated by the Bank of International Settlements and multiply the total obtained by three, with the argument that the wealthy hold only one third of their money as bank deposits. US economist Gabriel Zucman estimated more conservatively that total global funds held offshore to be $6.1 trillion, or 8% of global household wealth, by calculating the discrepancy between global assets and global liabilities i.e. money held the ownership of which is unknown "as if planet Earth were in part held by Mars." (Zucman 2015 p37). Zucman and Henry have criticised each other's methodologies, with Zucman's the only peer reviewed publication (Sunstein 2016).

Zucman also draws on a set of banking statistics only recently made available by the Swiss National Bank to calculate that $2.3 trillion in foreign wealth was held in Swiss banks in 2015. The ownership of 60% of this $2.3 trillion is attributed to secrecy jurisdiction such as British Virgin Islands, Panama, meaning that the origin of the money is unknown (Zucman 2015). $2.3 trillion is only just over one third of the total offshore wealth of $6.1 trillion, but Zucman argues the role Swiss banks is considerably larger, since large assets held in other offshore financial centres such as Singapore, Hong Kong, Bahamas, Cayman Islands, Luxembourg and Jersey are ultimately managed out of Swiss banks directly or indirectly. It is thus the behaviour of Swiss banks that has driven tax evasion, argues Zucman: "It is neither the involvement of the Virgin Islands or Luxembourg that enables tax fraud, but that of Switzerland (and comparable offshore private banking centers)" (Zucman 2015 p28).

In a paper on Russian-owned offshore wealth, Filip Novokmet Thomas Pikkety and Gabriel Zucman calculated total wealth held offshore by wealthy Russians equalled total domestic financial holdings. "There is as much financial wealth held by rich Russians abroad—in the United Kingdom, Switzerland, Cyprus, and similar offshore centers—than held by the entire Russian population in Russia itself" (Novokmet et al 2017 p5). In 2003 37% of FDI in Russia originated from the offshore zones Cyprus, BVI, Luxembourg, Netherlands and Switzerland (Haiduk 2007). In a more recent study, a team of geographers have examined the Russia-Cyprus relationship and 'round tripping': Russian-sourced investment re-invested in Russia as FDI via investment vehicles domiciled in Cyprus and other offshore zones (Ledyaeva et al 2015). In 2012, 61 percent of Russian outward FDI went to offshore jurisdictions, and 67 percent originated from them, with Cyprus accounting for the majority of the offshore flows, followed by the BVI, Switzerland, and the Netherlands.

2.4 Offshore in the mirror of investigative journalism: Panama Papers and Swiss banks

Journalists have also contributed significantly to the study of offshore finance and its centralities. Journalist William Brittain-Caitlin described the rise of the Cayman Islands as an OFC (Brittain-Caitlin 2005) while Gillian Tett narrated the rise and crash of credit derivatives in *Fool's Gold* (Tett 2010). Misha Glenny's investigative account of 'seriously organised crime' also reflected on the role of OFCs in mafia money laundering (Glenny 2008). Nicholas Shaxson's account of offshore finance, *Treasure Islands* (2011), has become a standard work for the broader public, putting the blame on the UK-USA for devising a system to siphon assets from developing countries to fund Western deficits. Shaxson argues that the Western-led anti-offshore campaign is hypocritical, aiming to prevent tax leakage from developed countries but not to prevent flows of illicit monies from the global south to developed countries (Shaxson 2011). The West's role in offshore finance rests on three pillars, according to Shaxson: firstly, what is known as the 'second British empire'. The second axis is via the US offshore states such as Delaware, and the US hedge fund industry operating out of the Cayman Islands (Shaxson 2011). The third pillar is the Swiss private banking sector. Switzerland operates on a far higher added-value rung of the offshore system, as one of the world's private wealth management systems, Shaxson argues. But the basic principles of secrecy and low tax remain the same as for the smallest of the 'treasure islands' (Shaxson 2011).

Shaxson and Oliver Bullough, a journalist who has reprised the topic more recently, both dwell on the trope of offshore as being nowhere but everywhere at the same time, as much a mode of being for the very rich than a geographical category:

> Offshore is not only a place, an idea, a way of doing things and a weapon of the financial industry. It is also a process: a race to the bottom to where the rules, laws and outward signs of democracy are worn away little by little (Shaxson 2011)

Bullough in turn calls it pithily *Moneyland* - defined with reference to Zucman as the missing 'land' that accounts for the excess of liabilities over assets in global finance, i.e. the place which owns the unattributed liabilities. Bullough covers much of the same ground as Shaxson,but adds a focus on how offshore finance is intertwined with oligarchic societies of China, Africa, Latin America and former Soviet Union. In contrast to Shaxson, Bullough not only refers to the financial underpinnings of Moneyland, but also to physical mobility of the superrich from outside the Global North (Bullough 2018)

> The laws of Moneyland are whichever laws anywhere are most suited to those wealthy enough to afford them at any moment in time. (…) They move their money, their children, their assets and themselves wherever they wish, picking and choosing which countries' laws they wish to live by. The result is that strict regulations and restrictions do not apply to them, but still constrain the rest of us (Bullough 2018 p27).

When in 2017 a hurricane hit the British Virgin Islands, it did less damage to the BVI's standing as an offshore jurisdiction than did the 2016 'Panama Papers' data leak of 4 terabytes of ownership data and related emails: the tax haven's standing depended on the regime of secrecy in combination with low taxes, not on physical infrastructure or even human capital (Bernstein 2017, ICIJ 2016). A key revelation of the 'Panama Papers' was the role of global banks, in particular Swiss banks, as buyers of offshore firms in bulk for their clients: "an offshore company without a bank account is of limited utility" (Bernstein 2017 p 186). Over 500 banks had ordered nearly 15600 offshore companies for customers from Mossack Fonseca, the company service provider that suffered the leak. One bank, HSBC, had ordered 2300 of these firms, mostly in bulk (Bernstein 2017). Even German state-funded banks were ordering Mossack Fonseca offshores en masse for clients. In a number of cases investigated by the journalists, the German banks had not correctly identified the beneficiary owner of offshore firms (Obermayer and Obermaier 2017). Other data leaks on offshore banking obtained by journalists have added to the picture of global banks as a driving force behind and source of custom for the flourishing of tax havens. Thus 'Swiss Leaks' revealed tax-evasion schemes operated through the Swiss subsidiary of HSBC that dovetailed with Panama Papers revelations, while the Paradise Papers exposed another offshore formation agent, Appleby, on the Bahamas, the billionaire clients of which originate from US and Europe, but also from the Middle East, China, former Soviet Union, Latin America and Africa (ICIJ 2015, ICIJ 2017).

2.5 Conclusion

As can be seen from the definitions provided for tax havens, OFC or secrecy jurisdiction over the last 25 years by scholars, the definition has remained largely the same from Hampton in 1994 down to Murphy in 2016, and remains focused on the 'tax haven' aspect of OFCs, i.e. regulatory mechanisms that provide zero tax and corporate secrecy to non-residents, ringfencing them from the onshore economy. This ringfencing of an offshore space turns OFCs into a space of exemption from domestic regulation for the non-residents who become their clients.

Table 2. Scholarly definitions of Offshore Financial Centre

a center that hosts financial activities that are separated from major regulating units (states) by geography and/or by legislation. (Hampton 1994 p237)
OFCs are places which host banking, insurance and other financial activities juridically away from onshore regulatory activities (Hudson 2000 p269)
Offshore banking refers specifically to financial operations designed to avoid regulatory and tax restrictions generally imposed by home governments (Warf 2002 p51)
Secrecy jurisdictions enable the creation of two distinct places, 'here' and 'elsewhere'. The former is a regulated, onshore, domestic space. The latter is the offshore space that is 'elsewhere'. Elsewhere is deemed by the secrecy jurisdiction to be somewhere distinctly different and outside its own domain (…) In the jargon of the offshore world that divide is a 'ringfence' (Murphy 2009 p2)
places or countries (not all of them are sovereign states) that have sufficient autonomy to write their own tax, finance, and other laws and regulations. They all take advantage of this autonomy to create legislation designed to assist nonresident persons or corporations to avoid the regulatory obligations imposed on them in the places where those nonresident people undertake the substance of their economic transactions. (Palan et al 2010, p8)
any jurisdiction through which financial claims pass to avoid policy constraints elsewhere (Cobham et al 2015 p241)

Secondly, the very debate over the term 'offshore financial centre' highlights the importance of reputation to the competitivity of OFCs. OFCs walk a fine line between providing customers with strong legal exemption from onshore constraints, while retaining a sufficiently good reputation to avoid damaging clients' onshore activities.

Thirdly, also connected to the discussion around the term 'OFC', there is a conflation of tax havens with financial centres: Some tax havens do not have a financial sector, let alone comprise a financial centre; many major centres of offshore banking such as Switzerland are not geographically offshore; the true centralities of offshore finance are the global cities. Fourthly, but in the same vein, there are close relationships between what Binder calls "offshore banking hubs" such as London, and tax haven jurisdictions where clients of such offshore banking hubs incorporate as special purpose vehicles, or shell firms (Binder 2019 p5). The latter have often been designed by banks or ABS in financial centres for use by their clients in combination with shell structures from other tax havens. Thus, a tax haven manifests itself not merely as a geographical and regulatory space, but in the specific legal vehicles that it supplies to clients of banking hubs.

Fourthly, the internal politics of OFCs tend to be oligarchic, in the sense of tight networks of insiders cutting across institutions making most outcomes predetermined. This means that regulators are often subservient to political necessity and given the overall importance of international reputation to OFCs, there is little tolerance for anyone 'rocking the boat' by questioning financial practices or launching independent investigations. Reputation overrides regulation.

I have also described how in the second wave of OFC research there is a shift in interest from the characteristics of individual OFCs to offshore as a category within globalised finance, given the role of banks in generating demand for offshore services. Thus, in geographers' accounts of offshore finance, emphasis has shifted from 'offshore' to 'finance'. The second wave created an awareness of the stickiness of the global offshore financial network, embedded in history, and the importance of the offshore supply-side, whereas the first wave focused on the demand side of footloose global funds in the context of globalisation.

Finally, I discussed how investigative journalism combined with large digital leaks of offshore data has lifted the veil on OFCs' tight links to global banks. This highlights that many clients of OFCs rely on no one more exotic than their bank manager to organise their offshore activity In the next chapter I will discuss scholarly approaches to regulation of the global network of offshore finance.

Chapter 3. The global Anti-Money Laundering regime and its critics

3.1 Introduction

As argued in the previous chapter, offshore finance is interlinked with the topics of illicit financial flows and money laundering. To combat these, in July 1989 the G7 group of leading industrialised countries founded the Financial Action Task Force on Money Laundering (FATF). At its founding, FATF was given a one-year mandate to design an international system that would stop narcodollars entering the banking system, since it was the US-led 'war on drugs' that had prompted the search for AML measures. Since that time, FATF has expanded to encompass most countries in the world, its remit extending to all crimes and even anticipated future crimes, and even to support global 'financial stability' (Nance 2018a). FATF's rapid and unexpected rise and expansion has caused a broad academic debate around what is known as the 'Global Anti-Money Laundering Regime' or also simply the 'FATF Regime'.

Despite its pervasiveness in popular culture, the concern about money laundering is relatively recent. Money laundering was only criminalised in the US in 1986, a pioneering piece of anti-money laundering (AML) legislation that was replicated in Switzerland as late as 2000 (Sharman 2017). Lexicological analysis shows that the term gained traction in the early 1970s, becoming popularised around the time of the Watergate scandal of the Nixon administration, where investigative journalists 'followed the money' trail from a burglary through to the White House (Sharman 2011). The apocryphal origin of the term is the time of Prohibition in the US when gangsters invested in the new business of laundromats to legalise cash from the illegal alcohol business during Prohibition (Nance 2018a). After the end of prohibition, 'money laundering' was mostly associated with illegal narcotics, the struggle against which was the origin of the FATF regime.

Interpol defines money laundering as "concealing or disguising the identity of illegally obtained proceeds so that they appear to have originated from legitimate sources" (Interpol 2020). Importantly, Interpol adds that the international movement of funds plays a key role in much contemporary money laundering: "Criminal gangs move illegally obtained funds around the globe using and abusing shell companies, intermediaries and money transmitters" (Interpol 2020). By the 1980s, the internationalisation of the drug trade made it clear that combating money laundering had to become a globalised task. In the first part of this chapter, I discuss what the FATF regime comprises and how it functions. In the second part I review the scholarly literature discussing the rise of the FATF regime, its effectiveness in combating money laundering, and its overall effects as a global governance regime.

3.2 Introducing the FATF regime

At its founding, FATF's original purpose was to establish international AML standards to combat laundering of narcotics revenues, in the context of the US-led 'war on drugs'. The founding summit called for "decisive action, both on a national and international basis to counter drug production, consumption and trafficking as well as the laundering of its proceeds" (quoted Sharman 2011 p26). The founding year showed how close international diffusion of norms and the exercise of military power accompanied each other: In December 1989 the US invaded Panama claiming the need to eliminate drug money laundering.

The establishment of FATF had followed the signing of the 1988 UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, known as the Vienna Convention (Reuter and Truman 2004). Negotiating the Vienna Convention had taken 10 years. A US participant to the negotiations told a researcher "I would rather have my teeth pulled out than to sit through another one of those negotiations" (Nance 2018b p114). It was understood that any effective AML regime would have to be both global in reach and able to enter countries' banking sectors – that is, be both extensive and intrusive. This would be unlikely to succeed without years of negotiations if drawn up as another convention or treaty.

Therefore, the informal ad hoc nature of FATF aimed to circumvent the usual diplomatic process and find a back door to quick worldwide establishment of an AML regime, leveraging the G7's financial power to do so. The very term 'task force' connoted that FATF was not to be a permanent organisation, but a forum to develop an international legal framework for AML (Heng and McDonagh 2008, van Duyne et al 2018). Though it is headquartered at, and has staff seconded from, the OECD's Paris headquarters, FATF is not formally part of OECD or any organisation (Gilmore 2011). It is not a legal entity and not registered in France: "The FATF is an informal club established by another informal club [G7]" (van Duyne et al 2018 p54-55).   FATF's main asset was not organisation, but the AML standards - the 40 Recommendations - that it compiled as a list and which were published in 1990 (Sharman 2011, Reuter and Truman 2004, Heng and McDonagh 2008). These are so important to the subsequent development of the FATF regime that I present them here in abbreviated form.

Table 3. The Forty Recommendations Of The Financial Action Task Force On Money Laundering (abbreviated from FATF 1990)

A. GENERAL FRAMEWORK OF THE RECOMMENDATIONS

1. Each country should implement the Vienna Convention and ratify it.
2. Financial institution (FI) secrecy laws should not inhibit implementation of these recommendations.
3. An ML enforcement program should include multilateral cooperation, mutual legal assistance, prosecutions and extradition in money laundering cases.

B. IMPROVEMENT OF NATIONAL LEGAL SYSTEMS TO COMBAT MONEY LAUNDERING

Definition of the Criminal Offense of Money Laundering

4. Each country should criminalize drug ML as per Vienna Convention.
5. Each country should extend the ML offense to all narcotics crimes
6. The ML offense should apply at least to knowing ML

C. ENHANCEMENT OF THE ROLE OF THE FINANCIAL SYSTEM

Scope of the Following Recommendations

9. Recommendations 12 to 29 of this paper should apply also to non-bank FIs.
10. The authorities should ensure broadest implementation of these Recommendations.
11. A working group could consider a common minimal list of non-bank and professions subject to these Recommendations.

Customer Identification and Record-keeping Rules

12. FIs should not keep anonymous accounts or accounts in fictitious names: they should be required (…) to identify their clients by personal documents and record that identity
13. FIs should learn the true identity of account holders where they suspect customers are not acting on their own behalf, especially shell companies
14. FIs should retain transaction records for five years

Increased Diligence of Financial Institutions

15. FIs should monitor complex, unusual large transactions and patterns of transactions lacking economic purpose.
16. If FIs suspect that funds stem from a criminal activity, they should report promptly their suspicions to competent authorities.
17. FIs should not warn their customers of such a report.
18. FIs reporting their suspicions should comply with instructions from competent authorities.
19. When an FI develops suspicions about customer operations, but cannot report them, it should close the accounts.
20. FIs should develop programs against money laundering.

Measures to Cope with Countries with No or Insufficient AML Measures

21. FIs should monitor transactions from countries not fully applying these Recommendations.
22. FIs should apply these principles to branches and subsidiaries located abroad, especially in countries not applying these Recommendations

Other Measures to Avoid Currency Laundering

23. The feasibility of measures to detect cash at the border should be studied (…) .

24. Countries should consider a system for FIs to report large cash transactions to a national central agency with a computerised database
25. Countries should encourage secure money technologies to replace cash.
Implementation, and Role of Regulatory and other Administrative Authorities
26. Bank supervisors should ensure that institutions have adequate AML programs.
27. Competent supervisors should be designated to implement these Recommendations in other professions dealing with cash.
28. The competent authorities should assist FIs in detecting suspicious patterns of behaviour by customers.
29. The competent authorities should prevent acquisition of FIs by criminals.

D. STRENGTHENING OF INTERNATIONAL COOPERATION

Administrative Cooperation (a) Exchange of general information

30. National administrations should consider recording international flows of cash in whatever currency to estimate cash flows from various sources abroad
31. International competent authorities (Interpol and the Customs Cooperation Council) should inform competent authorities about the latest developments in ML techniques
32. Each country should improve international information exchange relating to suspicious transactions, persons and corporations

Cooperation Between Legal Authorities

(a) Basis and means for cooperation in confiscation, mutual assistance and extradition

33. Countries should ensure that different standards in national definitions (..) do not affect mutual legal assistance.
34. International cooperation should be supported by a network of bilateral and multilateral agreements
35. Countries should encourage international conventions such as the draft Convention of the Council of Europe on Confiscation of the Proceeds from Offenses.

(b) Focus of improved mutual assistance on money laundering issues

36. Co-operative investigations between countries should be encouraged.
37. There should be procedures for mutual assistance in criminal matters regarding the use of compulsory measures
38. Expeditious action should follow from requests by foreign countries to identify, freeze, seize and confiscate proceeds based on ML and predicate offences
39. Consideration should be given to mechanisms for determining the best venue for prosecution
40. Countries should have procedures in place to extradite individuals charged with an ML-related offense.

In 1996, the 40 Recommendations were revised. Crucially, for the first time, the money laundering offence was expanded towards defining ‘all crimes’ as predicate offences – the original crimes that result in the need for laundering money - instead of the exclusive focus on drug money laundering. Whereas the original 1990 Recommendation Nr. 5 defined money laundering according to the Vienna Convention as “drug money laundering,” the 1996 version specified that “[e]ach country should extend the offence of drug money laundering to one based on serious offences” whereby each country would determine for itself which serious crimes should count as predicate crime for money laundering (FATF 1996). I discuss the timing of this decision to expand the definition of money laundering in the next chapter in connection with the illicit finance rippling out from the implosion of the Soviet Union.

The 40 Recommendations are written broadly to allow for leeway when transposing into individual countries' legislation (Nance 2018a). FATF standards have no formal binding force, not even on the G7 nations that founded it, hence they were published as 'Recommendations'. Nevertheless, they have been highly effective in having states across the world enact legislation to implement the norms (van Duyne et al 2018). FATF's power lies not in hierarchy but in its "transnational, multi-level network" which includes 34 FATF members and eight FATF-style regional bodies (FSRBs), which together encompass over 150 countries (Nance 2018b p115). Van Duyne et al compare the role of FATF in this network to a brand in a franchise business, whereby the brand is defined by the list of 40 Recommendations. This was confirmed indirectly by FATF executives. When revising the 40 Recommendations in 1996, FATF decided against changing the number of recommendations, because, as a FATF executive stated: the "40 Recommendations have become synonymous with the FATF and its mission," having gained "a measure of notoriety that has been helpful to the external relations effort," so that any change in the number would "adversely affect that recognition" (Gilmore 2011 p105).

The Council of Europe's Moneyval is an example of a FATF-style regional body. Historically the leading institutional role in combating money-laundering in Europe has been played not by the European Union, but by the Council of Europe. Following the collapse of the socialist bloc and the introduction of democracy and market-based economies within the former socialist countries at the start of the 1990s, the Council of Europe became the first major European body that these newly independent states could join, which in the process metamorphosed from a West European to a pan-European body. Given the Council of Europe's demonstrated commitment to AML, on one hand, and its expansion to include Central and Eastern European countries, this made it the natural vehicle for quickly implementing the FATF 40 recommendations throughout Europe, becoming the main partner for FATF in Europe. In 1997 it established a Select Committee for AML, later named Moneyval (Gilmore 2011).

The FATF toolkit: Mutual Evaluations, FIUs, and the Private Sector

One of the main activities of the FATF-affiliated regional bodies such as Moneyval was to organise its members states' Mutual Evaluations, a hallmark of the FATF regime. Mutual Evaluation was conceived in 1991 and the first round of FATF mutual evaluations concluded by 1996. A Mutual Evaluation combines peer review by experts from the member countries with on-site examination of an individual country's compliance with the 40 Recommendations. Scholars note that it is remarkable to have states assess each other's behaviour regarding a sensitive reputational topic such as money laundering. Mutual Evaluations are a "highly intrusive" process "without precedent in international practice in the criminal justice sphere" involving "the imposition of obligations which impact directly on the domestic criminal justice system of each participating state" (Gilmore 2011 p258). FATF's "invasive" monitoring powers are "among the farthest reaching of any international organization" (Nance 2018 p138). Accounts close to FATF view the acceptance of the Mutual Evaluation regime as one of FATF's major successes. (Gilmore 2011). More critical judgements, however, point to its circumventing democratic controls by national legislatures (Van Duyne et al 2018).

Financial Intelligence Units (FIUs) are another key component of the FATF regime. Although not directly stipulated in the original 40 Recommendations, FIUs developed in the 1990s as an institutional response to the requirement of Recommendation 16, in emulation of the US Financial Crimes Enforcement Network (FinCEN), established in 1989. FIUs have the function not only to receive and process suspicious reports domestically, but to coordinate and cooperate with their international peer FIUs internationally within the international Egmont Group of FIUs.

The third key novel component of the FATF regime was the direct involvement of the private sector in monitoring and reporting financial transactions. "In an unprecedented fashion" FATF argued that banks themselves had to play a major role in AML (Gilmore 2011 p95). This crucial decision to put banks "in the front line" against money laundering was motivated by the recognition that "[k]ey stages for the detection of money laundering operations are those where cash enters into the domestic financial system, either formally or informally, where it is sent abroad to be integrated into the financial systems of regulatory [tax] havens, and where it is repatriated in the form of transfers of legitimate appearance" (Gilmore 2011 p96). Thus FATF's intrusive harnessing of the private sector was thus from the outset aimed at controlling illicit offshore financial flows.

Overall the AML regime comprises two distinct components: prevention of money laundering and punishment for money laundering offences, or enforcement (Reuter and Truman 2004). The main pillar of prevention is the principle of Know Your Customer (KYC), also known as conducting due diligence on customers, which is introduced in Recommendations 12-14. Banks and other regulated financial institutions must ensure they know who their customers are, first and foremost by demanding and inspecting identity documents (Reuter and Truman 2004). In the case of business clients, the banks must identify the individuals who own the corporate entity, formally known as ultimate beneficial owners. Banks should also establish a profile of what they consider to be the normal financial activity expected of individual clients. In cases where the customer may count as a senior government official or its family, known as Politically Exposed Persons (PEPs), banks are required to exercise special care, termed 'enhanced due diligence' (Reuter and Truman 2004).

Where banks identify suspicious behaviour on the part of clients - such as large complex transactions with no clear commercial justification - they are required to file a suspicious activity report (SAR) to the appropriate national Financial Intelligence Unit (FIU) without alerting the customer (Recommendations 15-19). This reporting duty requires banks to appoint specialised AML officers, de facto creating a whole new profession in the financial sphere (Reuter and Truman 2004) (Recommendation 20). The national FIU receives and analyses these SARs and conducts its own investigations or passes them on to law enforcement. The FIU supervises banks' proper implementation of their AML responsibilities by monitoring their procedures, while liaising directly with banks' internal compliance departments (Recommendations 26-28). The FIU can sanction banks and other regulated entities, and even initiate prosecutions.

The second pillar of AML is enforcement, which focuses on 'predicate' crimes, the original criminal acts such as narcotics trafficking or extortion, of which money laundering is a derivative (Recommendations 4-6). Where the AML regime identifies suspicious transactions, enforcement tracks down any predicate crime from which the suspicious money might originate. While initially narcotics trafficking was the main predicate offence targeted by the FATF regime, in 1996 it was expanded to encompass all crimes producing illegal revenues both domestically and internationally (Reuter and Truman 2004, Sharman 2011).

The FATF 40 +9 recommendations envisage effective punishment for money laundering including not only imprisonment but also confiscation of the funds involved, and where possible their return to the original victim (Recommendation 30). The FIU and law enforcement can compel banks to waive banking confidentiality in order to share financial information on clients, and are required to cooperate both domestically and internationally (Recommendation 2, Reuter and Truman 2004, Sharman 2011).

3.3 Review of literature

The development of FATF was largely unexpected. As late as 1999, globalisation scholar Susan Strange described the FATF regime as a "pantomime" designed to satisfy public demands for action on drugs (Strange 1999 p126). Thus "arguably the primary theme" of research into the FATF regime discusses how it was able to expand worldwide so surprisingly and successfully:

> In 1990, an obscure, one-year task force published 40 vague and voluntary recommendations for building a better international anti-money laundering (AML) regime. In the intervening years, FATF has become the focal institution of a powerful financial governance regime (Nance 2018b p115).

Most scholarship tackling this first main question does so from the point of view of international relations theory, and thus not strictly pertinent to the current thesis. One body of thought argues that the successful establishment of the FATF regime was the result of its backing by both the US and the EU or, alternatively, by the US on its own (Drezner 2007, Simmons 2001). Nance argues in contrast that it was due to evolutionary and consensual 'experimentalism' involving social learning, where the threat of sanctions serves mostly to ensure parties persevere in dialogue with each other over improving standards (Nance 2018b).

Among these international relations approaches to FATF's successful expansion are those that draw on Foucaldian thought about the power of norms. They attribute the success of FATF expansion to the role of normativity in the FATF toolbox, using techniques such as mutual evaluations and 'name and shame' blacklists (Sharman 2011). This dovetails with scholarly discussion of the ‘FATF effect’ itself - the question of how and what FATF actually governs having attained global reach - and I discuss these approaches in more details below.

The second main research question in the literature, after the expansion question, is whether the FATF regime, having been successful in its expansion drive, is equally effective in achieving its goal of reducing money laundering. While this might seem an obvious question, some critics of FATF say there is a reluctance to answer it among AML experts. This reluctance in itself points to the power of norms within the FATF regime, which I will discuss below under the term ‘governmentality’. As early as 2004, scholars who questioned whether the AML regime is effective felt themselves questioning a taboo.

> Are AML rules really effective? After 15-20 years of setting standards it seems very hard to pose such a simple—and yet ‘subversive’—question. How could it become such a taboo? (Pieth and Aiolfi 2004 p415)

Critics of FATF argue that most research on the AML regime has been conducted from within what they call the ‘Laundering Dome’ of experts “accepting the prevailing basic premises and principals set out in the official discourse” (Van Duyme et al 2018 p321). In particular, the same scholars lament that there is no reliable data about how much money is laundered (Levi et al 2018):

> The [AML] system has managed to issue regular reports that include the word ‘evaluation’, an important label in contemporary policy circles, without in fact contributing much to knowledge of whether the FATF regime is indeed contributing significantly to global or even national wellbeing (Levi et al *op cit.*, p324).

Occasionally FATF allies such as Basel Institute of Governance’s AML Index also acknowledge that “there are no reliable quantitative data on money laundering available” (Basel Institute of Governance 2017). While FATF and its regional bodies produce copious quantities of evaluations, these assess compliance of states with the 40 +8 recommendations, rather than evaluating whether there has been an objective reduction in money laundering (Levi et al 2018). FATF, its regional bodies, and the national FIUs have become “profuse information disseminators” publishing hundreds of voluminous mutual evaluation reports, typologies and annual assessments (Van Duyne et al 2019 p16). But reports are often couched in opaque terms, and evaluations lack consistency (Van Duyne et al 2019).

A recent ‘critical handbook of money laundering’ thus poses the question of the AML regime: “What is all this good for? (…) What is the impact of the AML regime compared to the pre-AML state of affairs of unfettered money laundering?” (Van Duyne et al 2018). Sharman tried to answer this question by surveying egregious cases of kleptocracy, such as the Obiang family in Equatorial Guinea, and concluded that “there is little evidence to show that AML policy does work and a good deal to indicate that it does not.” (Sharman 2011 p164). The AML regime has successfully diffused internationally, but not because it is successful in combating money laundering. By 2013, even a leading academic policy advisor on AML in EU found that “money laundering is increasing rather than declining,” a fact described as a “ticking time bomb” (Unger 2013 p673). Such voices from within the ‘Laundering Dome’ remain rare, attesting to the marginalisation of criticism of FATF’s effectiveness as part of FATF’s inherent normalisation power, which I discuss next.

Governmentality and AML

The third main research question, and from the point of view of critical geography the most important question, is how and what does FATF actually govern? What is the FATF effect? Critical geography and international relations scholars have both approached this question by drawing on Michel Foucault’s conceptualisation of the interrelationship between norms and power in the modern age, which introduces the term ‘governmentality’ to denote “the conduct of conduct” (Dean 2010 p17). In this section I review these governmentality accounts of the AML regime, which form the basis for my analysis of the relationship between FATF and Latvia’s OFC in Chapter 6.

In contrast to the sovereignty of Machiavelli’s absolutist ‘Prince’, who is “unique in his principality and occupies a position of externality and transcendence,” Foucault argued that the concern of governmentality was not to control a territory and the subjects that belonged to it, but to govern a population (Foucault 1991 p91). Governmentality is a “question not of imposing laws on men, but of disposing things: that is to say employing tactics rather than laws, to arrange things in such a way that, through a certain number of means, such and such ends may be achieved” (Foucault 1991 p95). Governmentality decentred the conceptualisation of political power away from the “unified sovereign subject” towards disparate practices set in specific regimes such as prisons and science [Butler 2004 p52]: “[T]he tactics characteristic of governmentality operate diffusely, to dispose and order populations, and to produce and reproduce subjects, their practices and beliefs, in relation to specific policy aims" [Butler 2004 p52]. Power becomes a productive force that induces behaviour by establishing norms across discrete spheres of activities, rather than repressing behaviour via a catalogue of laws: "We pass from a technology of power that drives out, excludes, banishes, marginalizes, and represses, to a fundamentally positive power that fashions, observes, knows, and multiplies itself on the basis of its own effects (Foucault 2003 p48). A key concept in this context is a *norm*, a paradigm of behaviour applied as a metric to assess and to self-assess behaviour:

> the norm brings with it a principle of both qualification and correction. The norm's function is not to exclude and reject. Rather, it is always linked to a positive technique of intervention and transformation, to a sort of normative project (Foucault 2003 p17)

This means that 'normalisation' is the introduction of techniques that develop the self-governing capacities of individuals in a way that makes then participate in their own governance. As a result, power "is less (…) the imposition of a rule and more (…) the implication of a norm' (de Goede 2012 p87).

Governmentality has been fruitful as a critical concept both in international relations and in critical geography. In international relations, scholars applied this way of thinking to new forms of global governance and international regimes (Larner and Walters 2004). Human geography has a "thriving governmentality school" in regard to the implication of spatiality as a means of ordering and normalizing populations (Legg 2016 p860). In both cases, the FATF regime lends itself to the governmentality paradigm because of the role played by normalization and its decentralized modus cross-cutting between private and public sectors in finance. Theorists of transnational regimes such as FATF draw on Foucault to theorise about decentralised governance based on norms:

> [FATF] is best conceived, as argued here, as a Foucauldian governmental body that seeks to shape the 'conduct of conduct'. It 'governs' through the dissemination of knowledge-based technologies of government in the form of best practices, promoting learning and accepted benchmarks (…) in a whole lot of governance at multiple overlapping levels, affecting state learning, without a global Leviathan to compel compliance." (Heng and McDonagh, 2008 p572)

Sharman also sees governmentality as a promising approach to the AML regime:

> Governmentality suggests that rather than power being intentionally directed by the state, individuals can instead be induced to discipline themselves in a manner that does not involve deliberate calculation or even recognition. Power is fragmented and dispersed, working in and through practices and processes. In the context of global AML policy diffusion, this work makes much of the reliance on soft law, ranking and rating exercises, and the devolution of policy implementation to private entities such as banks. (Sharman 2011 p171)

Governmentality shifts focus from great power politics to the "boring everyday grind" (Sharman 2011 p172) of evaluations and international committee meetings, in turn influencing the "routine mundane activities" (Heng and Mcdonagh 2008 p 572) of high street banks, corner shops and remittance offices, Formally, compliance with the 40 Recommendations is voluntary, but in reality FATF members strive to achieve 'good marks' and positive reports from the FATF network (De Goede and Sullivan 2016). Member states compete amongst each other for grades (Heng and Macdonagh 2008). Implementing the 40 Recommendations comes to be seen as the 'thing to do', and the more countries adopt the policy, the greater the pressure to conform (Sharman 2011). But as I outline below, governmentality describes not only the expansion of FATF, also its very effect, what and how it governs: the FATF regime comprises a "practice of governmentality that enables unprecedented intervention into everyday financial life" (De Goede 2012 p35).

Governmentality, blacklisting and reputation: 'The bark is the bite' and 'Lists come alive'

Beyond the question of how effective or ineffective it is in combating money laundering, what is the overall 'FATF effect'? What and how does it actually govern? As shown above, the core of the FATF regime is not any hierarchical international organisation but a simple list of 40 recommendations, combined with an extensive and self-expanding network that references this list somewhat like a franchise chain.

A group of scholars have focused on the role played in the FATF regime of the technology of lists and blacklisting / greylisting / whitelisting. FATF's main means of influence is the threat of blacklisting of uncooperative jurisdictions. This is a threat to the crucial factor of reputation discussed in the previous chapter, through a process of 'name and shame,' but with no direct economic sanctions being triggered by blacklisting: "Blacklisting creates pressure to comply primarily by damaging the reputation of those countries listed among the international financial industry, and secondarily through creating fears of capital flight" (Sharman 2011 p99). The threat of blacklisting proved to be a potent means of diffusion because of the normative power - in the sense of both having moral properties while also establishing a benchmark for behaviour - that the AML regime accrued in the context of the 'war on terror'. In a study of how tax havens reacted to the threat and then reality of blacklisting by OCED, Sharman found that OECD wielded power in its very capacity to blacklist a state as a non-cooperative tax haven, without any accompanying sanctions. "The speech is the action, the bark is the bite" (Sharman 2009 p580). Blacklisting a state, as a speech act, in itself caused damage to a state so that they either amended their legislation as required before blacklisting occurred or after blacklisting.

> A German treasury official's comments were typical. When asked why states do not want to be blacklisted, he responded: 'Fear.' Why was there fear? Loss of reputation, [debt] ratings, a loss of image (Nance 2018b p134)

The role played by reputation in offshore finance, as discussed in the previous chapter, is of great significance in explaining why blacklisting has been so effective in coercing states into changing their legislation. Blacklists ripple out and magnify, because many states draw on the OECD and FATF blacklists when creating their own blacklists. Secondly, the blacklists changed the behaviour of private actors in the financial sector towards blacklisted jurisdictions, by raising the risk assessment for transactions involving these places. In particular, this applies to major correspondent banks' readiness to work with such jurisdictions. Sharman distinguishes between two routes that played out in connection with the threat of blacklisting, ex-ante and ex-post. Low-level tax havens serving mostly private individuals, such as Cook Islands, Kitts and Nevis, and Vanuatu, complied with OECD and FATF demands only after being blacklisted, after subsequently experiencing financial losses. Jurisdictions that provided services to financial intermediaries, such as Cayman, Austria, Mauritius and the Isle of Man, complied with demands after the mere threat of blacklisting was made, anticipating future financial damage given the high sensitivity of institutional investors to reputation (Sharman 2011).

Moving back onshore, Leyshon and Thrift examined how the use of software-supported lists in financial credit scoring makes “lists come alive”, pointing to “a new form of governmentality within the [banking] industry which is founded primarily upon computer software” (Leyshon and Thrift 1997 p435). While lists are an ancient organisational technology, a crucial new factor regarding lists and governmentality is speed of processing when combining lists with IT. IT turns lists into databases, “carefully arranged lists, digitalised to take advantage of the electronic speed of computers” (Leyshon and Thrift 1997 p442). Lists “come alive” because they are constitutive of new spaces of financial inclusion and exclusion, and so “have the power to include or exclude individuals from the financial system itself” (Leyshon and Thrift 1997 p442). The power of lists extends even to filtering of incoming calls for customer service according to data maintained on the commercial attractiveness of the user of the telephone number. At the same time, this transformation was unfolding with little attention because such “new practices of knowledge […] are written into the rules of procedure followed in the writing of software and are therefore rarely examined.” (Leyshon and Thrift 1997 p435). Bank retail software is effectively a black box removed from social scrutiny that replaces the community knowledge of bank managers (Johns 2016, De Goede 2016).

In this way, in governmentality, lists replace laws. De Goede et al similarly argue that lists and listing are intrinsic to governmentality:

> … listing is a performative technology that helps constitute the objects and categories it targets or compiles. While the list appears as a simple instrument to execute prior legal decisions, […] it does much more: it creates juridical spaces and connects legal actors in new ways. […] the list has become not just a conduit but an active participant in contemporary governance (De Goede et al 2016 p6).

As a form of knowledge, argues de Goede, “lists privilege overgeneralised schema through de-contexualisation and the use of simplified formatting” (de Goede and Sullivan 2016 p70). This leads to a reification of the list as fact, despite doubts about the quality of intelligence on which a list is based: “a list produces a reality of its own - it is seen as a self-evident and clean fact where the traces of its production have become invisible” (Stäheli 2016 p15). Thus, according to De Goede and Sullivan, the UN Al-Qaeda sanctions list as incorporated into UK law

> … does more than compile and classify pre-existing elements from an entity called 'al Qaeda'. The list 'comes alive' as an actant, constituting al Qaeda itself as a more or less coherent global terrorist network to be countered" (de Goede and Sullivan 2016 p70).

Another aspect of lists is that they are a preemptive measure. Therefore, they are situated outside the usual framework for law enforcement. They are often the result of collaboration among multiple agencies, whereby the criteria of selection for the list may not even be clearly and consistently defined. Since lists are so easy to apply, there is little restriction placed on the scope of lists. Some lists, such as the Terrorist Identities Datamart Environment (TIDE), administered by the US National Counterterrorism Center, ran to over 1.1 million entries in August 2014. It is used to compile no-fly lists running to 119,000 individuals (de Goede and Sullivan 2016). Moreover, there is a proliferation of private-sector lists as part of AML technologies and of software that integrates lists into master lists (de Goede and Sullivan 2016). There are few channels for individuals placed on such lists to appeal against the decision. De Goede discusses the case of a Stanford University student who was placed on the list by human error, and only after eight years of litigation was removed, but remained included on other derivative lists, preventing her from obtaining a US visa (De Goede 2016). A single list, such as a no-fly list, is potentially coupled to multiple additional lists rippling out as it is processed through further databases (John 2016).

While most research on lists has focussed on blacklisting, as described above, there are also studies of whitelists - lists of entities that are pre-approved, automatically accepted, flagged through without checks or questions: "whitelists [have] a form of 'agency' (…) they can make things happen and can therefore also be held co-responsible for political developments (Leander 2016 p62). Whitelists are defined in one account as "classification systems and technologies that pre-authorise action or access for entities judged to be safe or trustworthy" (Bedford 2016 p31). Whitelists in AML regulation can "involve place-based judgements about trustworthiness" and "purport to classify trust, worthiness, and reputation, and organise collective feelings of pride" (Bedford 2016 p35). While both blacklists and whitelists "offer special treatment based on accumulated reputational capital," the difference is that "[t]ypically whitelists appear a fairer, more moderate, and indirect technique for changing conduct than blacklists, in part because they rely on and help to pass on 'good' feelings, atmospheres, and orientations around trust, pride, and inclusion" (Bedford 2016 p33, p35).

For instance, a study of a British whitelist of jurisdictions for online gambling providers showed how politicised the list quickly became. The original policy was that the whitelist should include only jurisdictions that had the same online gambling standards as UK legislation. However, it proved possible after lobbying for low tax ‘offshore’ jurisdictions such as Gibraltar to be included on the whitelist, while a Canadian First Nation jurisdiction was excluded despite having equivalent standards (Bedford 2016). Finally, the whitelist admitted the Carribean jurisdiction of Antigua and Barbuda - one of the pioneers of international gambling sites in the 1990s - despite significant misgivings among MPs. As a result, the decision was taken to cancel the whitelist altogether. Bedford’s paper exposed the racialised dimensions of blacklisting and whitelisting, showing how these terms are embedded in “colonially structured racialised distinctions between trustworthy and suspicious places and peoples” (Bedford 2016 p43). In Chapter 6, I resume and expand this discussion of blacklisting, greylisting and whitelisting to examine the strategies and effects relating to the successful avoidance of blacklists and greylists within the FATF regime, which I refer to as de facto ‘whitelisting’.

Lists and banks

A growing number of scholars have conducted fieldwork in the banking sector to explore how AML technologies such as lists work in practice. Amicelle and Jacobsen (2016) confirm that the “list appears to have become the security device of choice in the everyday life of the financial industry across the world” (Amicelle and Jacobsen 2016 p89). Databases integrate voluminous lists of politically exposed and / or sanctioned individuals and companies worldwide, with alone a list of the list titles running to 37 pages, whereby the longest single list runs to 1.3m entries (Amicelle and Jacobsen 2016). List-based transaction screening software means that banking activities are recast as security problems, while bank officers take decisions on security matters, for instance adjusting filters on screening software to reduce the number of false positive results.

Favarel-Garrigues et al (2007) explore the new relationship between banks, law-enforcement, and the French Financial Intelligence Unit, Tracfin. Their research focuses on the compliance officers, i.e. the bank employees now tasked with AML. Having previously had “normal duties (…) oriented toward commercial activities based on a high regard for privacy,” they were now “led to assume police duties,” and enjoy “powers that are wide-reaching but hidden” (Favarel-Garrigues 2007 p1). This transformation encapsulates the installation of a governmentality regime into personal finance:

> The originality of these apparatuses lies in their introduction of the state into the surveillance of what had previously been a strictly private interaction, regulated by contractual relations of confidentiality and non-intervention. This is indeed the realization of ‘governmentality at distance’ and converges with how Foucault conceived power, not as a possession that is conquered or that one appropriates, but as a relationship, a series of continuous interactions between an authority (a governing entity) and subjects (the governed) (Favarel-Garrigues et al 2011 p181).

Antoinette Verhage also focuses on compliance officers as “one of the new actors in the policing landscape [who] adds to the multilateralization of policing” (Verhage 2012 p15). She describes some aspects of the intrusion of law-enforcement roles into the private sector as the ‘big brother’ model, quoting one of her respondents saying that the cumulative effect of surveilling clients’ financial behaviour on daily basis was similar to being in the feared East German secret police, a “true Stasi-situation” (Verhage 2011 p75). As noted above, despite use of screening software, compliance officers in banks still have considerable powers of discretion, for instance deciding at what level of seniority does an official count as a PEP (Verhage 2011).

Verhage discusses the triangular relationship between banks, regulators and private firms in the ‘compliance sector.’ Regulators require use of blacklists for transaction monitoring, creating a captive market for the private firms that supply them to banks. Verhage calls for the state itself to compile and supply a comprehensive blacklist to the private sector, in order to avoid the “commoditisation” of such highly sensitive personal data (Verhage 2009 p388). However, there is already one list that is dominant in the market: World-Check, the largest commercial database on individuals and entities (Tsingou 2018). World-Check lists all ‘politically exposed persons,’ i.e. current and former office holders, as well as businesspersons and company officers with any negative media or legal record, as well as sanctioned individuals and entities, backed by inhouse research. Because “a large majority of financial institutions [buy] these products, the software leads to increased standardization of AML practice” (Tsingou 2018 p197). This standardisation of lists in the form of World-Check is part of the emergence of the new profession of ‘compliance’. Thus, lists do not just define those categorised therein, they also define and discipline the profession of those who are using them, part of the rise of the "new governors" (Tsingou 2018). I discuss World-Check again below.

From AML to AML-CFT

In October 2001, following the 9/11 attacks on the World Trade Centre in New York, FATF introduced the 9 Special Recommendations on Terrorism Financing as a supplement to the original 40 Recommendations, which changed the AML regime into an Anti-Money-Laundering / Combating the Financing of Terrorism regime (AML/CFT).

Table 4. FATF IX Special Recommendations on Terrorism Financing (FATF 2001)

1. Each country should take immediate steps to ratify and to implement fully the 1999 United Nations International Convention for the Suppression of the Financing of Terrorism and the United Nations resolutions relating to the prevention and suppression of the financing of terrorist acts
2. Each country should criminalise the financing of terrorism, terrorist acts and terrorist organisations. Countries should ensure that such offences are designated as ML predicate offences.
3. Each country should implement measures to freeze funds of or for terrorists in accordance with the United Nations resolutions relating to the prevention and suppression of the financing of terrorist acts.
4. If FIs suspect that funds are linked to terrorist activity, they should report their suspicions to the competent authorities.
5. Each country should maximally assist another country with investigations relating to the financing of terrorism. Countries should also not provide safe havens for individuals charged with the financing of terrorism.
6. Each country should licence services for the transmission of money or value, and subject them to all the FATF Recommendations, and sanction illegal services.
7. Countries should require FIs to include accurate originator information on funds transfers and the information should remain through the payment chain.
8. Non-profit organisations are particularly vulnerable to abuse for financing terrorism, and countries should ensure that they cannot be misused
9. Countries should monitor the physical cross-border transportation of currency including a declaration system with sanctions for false declaration

Because the aim of the measures was to prevent terrorism, the 9 Special Recommendations introduced a pre-emptive element into the FATF regime, henceforth reborn as AML-CFT. Special Recommendations 1-4 aimed to track financial flows in anticipation of a terrorist offence, i.e. pre-emptively. De Goede uses the term 'Speculative Security' to denote a security regime that acts pre-emptively. Expanding FATF's role to the preventive logic of anti-terrorist financing amounted to a watershed in FATF's international role (de Goede 2012). The link to anti-terrorism enhanced FATF's international standing just as its remit was greatly expanded. Combating terrorism financing - preempting the use of possibly legally obtained and relatively small sums of money to commit a criminal act - was the opposite of combating laundering of narcotics revenues, the original purpose of FATF; that is, the concealment and legitimization of the large-scale proceeds of a crime already committed (de Goede 2012). AML-CFT thus introduced a surveillance regime to the global financial system, leading to a proliferation of offices involved in the "technical and seemingly apolitical work of commercial risk managers, software models, and compliance officers" (de Goede 2012 p55). De Goede terms the new expanded AML-CFT regime the "security-finance assemblage": a "transnational landscape of laws, institutions, treaties, and private initiatives that play a role in fighting terrorism financing" that regulate "the minutiae of everyday life, including ATM transactions, wire transfers" (de Goede 2012 p28-29) and "lays out new normalities concerning everyday financial behavior" (de Goede 2012 p46).

De Goede details how this security-finance assemblage is expansionist, intrusive and unaccountable. De Goede analyses the 'Terrorist Finance Tracking Program,' known as the 'SWIFT affair' (de Goede 2012 p59). In 2006 it was revealed that the US, in the aftermath of 9/11, had subpoenaed data on millions of international wire transactions from the Belgium-based Society for Worldwide Interbank Financial Telecommunications (SWIFT), as part of a self-explanatory US program called Terrorist Finance Tracking Program (TFTP). A designer of TFTP claimed using the data would create "a unique and powerful window into the operations of terrorist networks" (de Goede 2012 p68). De Goede argues that analysis of links between individuals based on such financial data leads to "criminalization of association in public life […] Who decides where the boundaries of suspect networks are?" (de Goede 2012 p68).

A second example of overreach by the AML regime was the post 9/11 AML regime focus on informal remittance systems such as hawala, which are cash-based and often do not have even paper records of transactions, let alone standardised electronic records like SWIFT. The suspicion of hawala as a mode of terrorism financing emerged in the immediate aftermath of 9/11, both in the form of sensationalist media coverage and political action (de Goede 2012 p99). Thus, Special Recommendation 6 calls for increased regulation of alternative remittance networks such as hawala. However, the authoritative report on 9/11 established that hawala transfers played no role in the financing of the attacks, which were funded by money provided through legitimate bank transfers (de Goede 2012). The suspicion of hawala thus reflected the paradox of AML-CTF: as the FATF's report on terrorism financing noted: "In many situations, the raising, moving and using of funds for terrorism can be . . . almost indistinguishable from the financial activity associated with everyday life" (de Goede 2012 p27).

The Anti-kleptocracy Regime

While De Goede portrays how pre-emption of terrorism permeated the AML regime after 2001, Sharman describes how of the AML regime also latterly expanded into restorative anti-kleptocracy, its third incarnation alongside the 'war on drugs' and the 'war on terror'. While De Goede's 'security-finance assemblage' conducts pre-emptive tracing of funds before a crime occurs, the anti-kleptocracy regime traces funds believed to result from corruption and embezzlement by ruling groups, even where has been no criminal investigation or charges brought for specific offences. Thus, the anti-kleptocracy regime comprises a further expansion of the remit of the FATF regime.

The anti-kleptocracy regime dates to the mid-1990s when, as I discuss in the next chapter in more detail, Western states, in particular the US administration of Bill Clinton, initiated action against grand corruption, prompted in particular by new concern about illicit outflows from the former Soviet countries (Sharman 2017). Sharman argues that that the US has been a powerful force in the anti-kleptocracy regime, but that the anti-kleptocracy regime cannot be reduced to US hegemony or power interests. It was only in the 1990s under the Clinton administration that the 1977 Foreign Corrupt Practices Act (FCPA) began to be strictly enforced. Given this new focus, the US Senate sub-committee on investigations under the chairmanship of Carl Levin embarked on a program of investigating the laundering of foreign corruption revenues in the US financial system, lasting from the late 1990s until his retirement in 2014. With powers to subpoena bank records, the subcommittee investigated Citibank, Rigsbank, and others, uncovering funds held by foreign rulers that were incommensurable with their official incomes. In connection with this, the US launched successful prosecutions of a succession of foreign statespersons from Peru and Ukraine.

The centrepiece of the new international anti-corruption regime became the United Nations Convention against Corruption (UNCAC), which entered into force on December 14, 2005. The UNCAC provides for enactment of new measures such as wealth declarations by officials and sanctions for false declarations, while building on the FATF AML regime and its principles such as KYC. “Many of the specific measures (…) restate existing soft law principles designed by the Financial Action Task Force to counter money laundering” (Sharman 2017 p48). It also lays down the principle of assets being returned to looted countries (Sharman 2017). The anti-kleptocracy norm of holding national leaders to international account for corruption crimes voids a centuries-old principle that sees incumbent heads of state as enjoying international immunity while in office (Sharman 2017).

Sharman highlights the example of Switzerland to underscore the paradox of anti-kleptocracy: Switzerland has repatriated more laundered money than any other country, to countries such as Angola, Argentina, Brazil, France, Germany, Italy, Kazakhstan, Mali, Nigeria, Peru, the Phillipines, Spain, Ukraine and Russia. As Sharma argues, “it is almost easier to list the grand corruption cases that do not have a Swiss connection than all those who do” (2017 p91). But the volume of repatriated assets indicates that Switzerland remains a global safe deposit box for kleptocrats, at least until they lose power. Thus, while the AML-CFT regime searches for the needle in the haystack of terrorism funding, it fails to see the elephant in the room of kleptocractic flows of money, pointing again to the lack of effectiveness of the AML regime. “Because prevention is a far more effective means of combating corruption than the long expensive and uncertain path of asset recovery, this gap constitutes a crucial flaw, even if we take into account the accounts of stolen wealth returned from Switzerland” (Sharman 2017 p117).

3.4 Conclusion: Bringing money laundering back in to the study of AML

In this chapter, I have surveyed the scholarly debate on the FATF regime as informed by Foucauldian ‘governmentality.’ This pertains firstly to the undisputed, if unexpected, success of FATF in expanding to encompass most countries around the globe, despite its intrusive nature. A major part of this success is attributed to FATF’s normalising technology of blacklisting and greylisting countries failing to implement its ‘recommendations.’ This technology reprises the theme of reputation as important to OFCs that I examined in the previous chapter, and which will form the basis for my analysis in Chapter 6 A second smaller strand in the literature examines whether FATF is actually effective at reducing money laundering. While there is little reliable data, frequent revelations in media and politics about large-scale money laundering suggest that FATF has not significantly reduced money laundering. This then raises the question of the 'FATF effect': How does the intrusive FATF regime impact on global financial geography and practices?

One of the main themes in the literature is that FATF and the broader AML-CFT regime governs through wielding lists - blacklists, greylists, whitelists, kill lists, no-fly lists, sanction lists - rather than laws. Because of the unaccountability of such list-making, countries, entities and individuals are concerned to avoid even the possibility of listing, thus prompting a heightened care for reputation and rankings. Part of the FATF effect, from a governmentality perspective, is thus the constant care of reputation and legitimacy in global finance on the part of countries and companies, in connection with the proliferation of various indices of compliance. At its worse, the AML-CFT regime is restrictive of rights and destructive of privacy. The question thus arises whether such anti-democratic features of AML-CFT are justified by the gains in combating illicit finance, in particular illicit offshore finance, given the threat to democracy posed by the latter discussed in the introduction?

This question however remains unanswered given the consensus among scholars reviewed here is that there is a shortage of data, and thus a need for research, on the extent of money laundering, i.e. there is a need for researchers to bring money laundering back into the study of anti-money laundering. "Research and analysis that focuses on direct measures, however, remains the exception to the rule" (Nance 2018a p148). Nance, for instance, proposes researchers track how the price charged by money launderers responds to AML efforts (Nance 2018a). Sharman has already introduced innovative methodology, such as testing how easy it is to incorporate shell firms for money laundering across the world, and hiring a private detective to sift through property records in Australia to identify kleptocrats (Sharman 2011, 2017). These attempts, while promising, remain insufficient. In the next chapter I will introduce my methodological approach to fieldwork in money laundering, and present my research project focused on delineating the 'FATF effect' on money laundering, thus attempting to 'bring money laundering back in' to the scholarly discussion of the FATF and AML regimes.

Chapter 4. Research design and methods

4.1 The research question and design

This chapter introduces the research question, based on a research deficit identified in the previous two chapters: the impact of AML on the geography of illicit offshore finance. I explain the choice of Latvia as a case study suitable to research this question. Then I describe my methodology, comprising of interviewing, on the one hand, and the use of digital data on the other. Finally, I discuss the ethical issues connected with these approaches and issues of my positionality to the research topic.

The discussion in the previous chapters revealed a research deficit concerning the impact of the global AML regime on the geography of illicit offshore finance, i.e. examining the interaction between the FATF regime reviewed in Chapter 3 and OFCs as reviewed in Chapter 2. There is a need to ‘bring money laundering back in’ to the study of anti-money laundering. With some exceptions listed above, academic research on OFCs has produced little data on illicit financial flows, while scholars of AML have themselves called for more research on money laundering. In investigative journalism, the situation is different due to the use of data leaks such as the Panama Papers. However, as Levi et al argue, these focus on celebrity cases and frequently become part of the “claims-making process” regarding money laundering instead of being used for sober scholarly assessment (Levi et al 2018 p309).

This research gap is important for a number of reasons. As argued in the introduction, the goal of FATF to combat illicit finance is crucial in reducing corruption and safeguarding democracy, so it is important to know whether FATF can attain its goals, or whether illicit money flows unabated? Dark money from illicit finance undermines democracy while strengthening authoritarian kleptocracies. Is the FATF regime successful in reducing this phenomenon? Secondly, as we have seen in the previous chapter, AML - CFT is a global surveillance regime with low democratic accountability and high intrusiveness. Thus privacy and rights are sacrificed with reference to the need to combat money laundering. So the question is: does FATF combat money laundering effectively enough to justify the scale of intrusion on individual lives by the FATF regime? This question can only be answered by bringing money laundering back into the study of AML.

Because the research question of the impact of the FATF regime on the geography of illicit offshore finance relates to qualitative aspects of money flows - whether clean or dirty money - it requires painstaking qualitative analysis. Thus, in the framework of a doctoral thesis it makes sense to restrict the analysis to one financial centre. The case study has a long tradition in economic geography and more broadly qualitative social science (Flyvbjerg 2011). As shown in Chapter 2, case studies were typical for the 'first wave' of studies of offshore financial centres, which focused strongly on aspects of place, in particular competition among places in terms of reputation, regulations etc.

4.2 Selecting Latvia as a case study

It makes sense for a case study to focus on an aspect of post-Soviet offshore finance, given the role that the collapse of the Soviet Union played in the expansion of FATF from an anti-narcotics tool in 1990 to the present day 'all crimes' ML offence established in 1996. Firstly, the end of the Cold War, as has often been noted, meant that the West no longer supported criminal regimes simply because they were anti-communist, while support from the Soviet successor states for the former Soviet client states had evaporated (Heywood 2018). This meant that the political tolerance in the West for cross-border crime and corruption sank.

On the other hand, as discussed briefly in Chapter 1, the collapse of the Soviet Union and subsequent integration of the successor states into the capitalist global system led to huge and largely illicit outflows from the successor countries to offshore jurisdictions such as Switzerland (Novokmet et al 2017). Thus the collapse of the Soviet Union led to AML and anti-corruption becoming a priority policy for the US and allies in the G7 and OECD beyond its anti-narcotics campaign. The fight against transnational crime became America's new mission, as expressed in 1997 by then Senator John Kerry, a close ally of the Clinton administration. Emphasising how organised crime was "hijacking the Russian bear," he wrote in his book 'The New War' that "America has no choice but to lead the world against private criminal enterprises as it led the world against public criminal governments. (…) We need to create a new international alliance to meet the threat like the alliances that defeated Fascism, Communism and Saddam Hussein" (Kerry 1997 p32). Kerry said that the Russian government was synonymous with the Russian mob and that huge smuggling operations saw metals and minerals flooding out of Russia via Baltic ports. The renewed threat of transnational organised crime arising in the aftermath of the Soviet collapse, ranging from human trafficking to proliferation of weapons of mass destruction and kleptocracy led to an "explosion of international policy making on this front in 1994-1997" (Sharman 2017 p41). This was also reflected in US policy discussions around the 'dark side of globalisation' that resulted in the creation of a US National Security Council directorship for transnational threats headed by a Russia specialist (Clinton White House 2000, Farah and Braun 2007). The second half of the 1990s saw the first major US transnational investigations and prosecutions, many linked to post-Soviet space, such as of Russian arms trader Viktor Bout, organised crime figure Semion Mogilevich, Ukraine's prime minister Pavlo Lazarenko, and the Russia-linked Bank of New York (BoNY) scandal (see next chapter).

It was thus against the background of the collapse of the Soviet Union and its chaotic aftermath that the FATF regime expanded in 1996 from anti-narcotics to an 'all crimes' AML regime. The commentary to the 1996 revisions noted that this revision was "without question the most critical one":

> [O]verwhelming evidence in FATF countries and throughout the rest of the world that non-drug predicate offences constitute an important and growing source of illegal wealth entering legitimate financial channels. Indeed, in some countries non-drug related crime constitutes the predominant source of laundered proceeds. (FATF 1996 p7)

Therefore, although FATF was conceived shortly before the collapse of the Soviet Union, it was effectively refunctioned from the 'war on drugs' to the present day sweeping 'all crimes' basis in the wake of the Soviet collapse. Thus to assess the impact of the 'all crimes' AML regime on offshore finance, it makes sense to look at offshore flows connected specifically to the former Soviet Union.

The case I have chosen in order to examine the impact of AML on illicit offshore finance is that of the post-Soviet country of Latvia, specifically the offshore financial sector in its capital Riga. Riga is the only financial centre to have moved from being part of the Soviet Union and then implicated in the illicit dollar financial flows of the immediate post-Soviet years, to joining the EU and NATO by 2004, the Eurozone by 2014 and the OECD by 2016, and in the process adopting AML institutions and practices. This makes it a suitable test case for the impact of the FATF regime on illicit offshore financial flows.

In his influential article on case studies, Charles Ragin proposed that a researcher should follow a hierarchy of casing, leading from theory to case study, as a way of bridging "the equivocal nature of the theoretical realm and the complexity of the empirical realm (…) to make the linking of ideas and evidence possible." While I do not share Ragin's positivist epistemology, the 'hierarchy of casings' he proposes is a useful tool to think about the selection of a case study. Proceeding along the same lines for my case study of Riga, the hierarchy of casing would look thus:

Table 5. Casings of research project

Casings of my research project	Hierarchy of casings (Ragin and Becker 1992)
(1)A case study of illicit global finance	(1) The most general level
(2) A case study of offshore financial centres and FATF / AML	(2) A subset (historical, developmental and conceptual)
(3) A case study of post-Soviet offshore flows	(3) Theoretically motivated narrowing of empirical focus
(4) A case study of offshore banking in Latvia	(4) Selection of main empirical samples
(5) A case study of 1992-2018	(5) Selection of empirical evidence to be collected

The research questions that I pursue using the case of Riga / Latvia, corresponding approximately to the four results chapters are thus:

1) How did the financial sector emerge in post-Soviet Latvia? What was its connection to money laundering and illicit offshore finance in the 1990s?

2) How was AML implemented in Latvia?

3) How did banking practices and offshore money flows change in connection with implementation of AML?

4) What other international regulatory measures were applied to Latvia / Latvian banks because of illicit flows? What was the driving force behind these measures?

Case studies and assemblage theory

While Ragin and Becker use case studies to exemplify a body of theory in a positivist fashion, my understanding of a case study is informed by post-structuralist theory, in particular assemblage theory as formulated by Saskia Sassen in the new sociology of finance, in turn strongly influenced by Actor-Network Theory (ANT). While it is not possible here to trace the intellectual history of these approaches, suffice it to say that assemblage theory eschews an explanatory evidential-based approach for a descriptive ethnographic approach where the case studies are in themselves their own explanation (Law 2009). Empirical work becoming manifest in case studies comprises the methodology of an assemblage approach:

> [I]t is not abstract but is grounded in empirical case-studies. We can only understand the approach if we have a sense of those case-studies and how these work in practice. (Law 2009 p141)

Proceeding from this logic, the focus on offshore banking in Latvia is an access point from which to trace out an assemblage encompassing global financial circulation and regulation thereof.

We can note here that the term 'assemblage' has developed with two theoretically related but distinct usages (Muller and Schurr 2016). The first usage, originating in the ANT tradition, focuses on actual existing connections and constellations at a given point in time. The second, inspired by the original usage of the term 'assemblage' in the works of Deleuze and Guattari, pays more tradition to the flux and ruptures of time, including potential and virtual dimensions (Muller and Schurr 2016). These usages have often been distinguished by the clunkier terms of actor-network in the first case, and agencement in the second. Despite these differences, scholars point to major overlaps between the use of assemblage to denote actor-network, and assemblage denoting agencement.

> both have a relational view of the world, in which action results from linking together initially disparate elements. Both emphasise emergence, where the whole is more than the sum of its parts. Both have a topological view of space, in which distance is a function of the intensity of a relation. And both underscore the importance of the

> socio-material, i.e. that the world is made up of associations of human and non-human elements (Muller and Schurr 2016 p226).

The strongest criticism of assemblage in the sense of ANT is that there is too strong a focus on stability, and a neglect of power relations behind such stability, resulting in implicitly conservative politics (Muller and Schurr 2016, Legg 2007). In this thesis, I follow Saskia Sassen's use of assemblage, which aims to overcome such failings. While using assemblage in a sense more aligned with ANT, she retains its critical import by emphasising the hybridity and thus instability of networks. By tracing assemblages of hybrid elements, Sassen seeks to interrogate conventional terms and paradigms by showing their dependency on phenomena apparently marginal to them. Thus far from assemblage denoting a stability, by fully tracing a network to include the apparently marginal, she uses it to destabilise accepted understandings: "I have long seen the rise of new types of formations beneath familiar events, and beneath the general language deployed by the social sciences" (Aneesh 2017 p129). According to Sassen, assemblage thus denotes the networking of the socially dominant with exploited, marginalised and excluded.

> I am far more interested in the ambiguous, often weak, edges of the paradigm, than in its strong centre (…) A simple image: strong light on a street on a dark night; the stronger the light, the more I see what is inside the circle of light and the more difficult it is to see what lies in the penumbra around that circle of light. (…) A second marker is the need to actively destabilise existing categories and definitions (…) One simple illustration: 'The' economy—what does the formal category with its specific obligatory measures and interpretations of those measures, actually not include. . .such as the very long term-unemployed, the growing stretches of dead land that reduce the operational field of an economy, the survival tactics and practices of the displaced that often entail the need to make an economy? (Aneesh 2017 p129)

In this respect, a 'assemblage' case study aims to deconstruct politically dominant categories by showing their networking with marginalised, peripheral phenomena. Thus relations appearing stable are shown to be based on conflictual power relations and marginalisation practices.

While my case study addresses the research questions as outlined above, it is also conceived as a study of a specific and under-researched type of offshore financial centre specialised in the shadow economy. This responds to recent calls for enquiry into how individual financial centres provide specialist functions. While it is accepted that "[e]ach of the leading financial centres has developed its own specialised advantages over the last two decades," scholars have also pointed to the proliferation of new secondary financial centres, each with their own specialisation, many of which are outside the global north and should be treated in their own terms (Sassen 2012, Hall 2018, Muller 2018).

4.3 Interviewing elites in Eastern Europe

Semi-structured elite interviews play a key role in both assemblage theory as well as in the sociology of finance. Assemblage theory seeks to find out what actors do and thus to trace their networks, rather than to explore their agency. Thus interviews are geared towards network tracing rather than 'opening a window on the soul'. "By mobilising key informant interviews it is possible to identify and trace elite human actors, as well as access non-human actors (Ruming 2009, p458). Sociology of finance, for which the trading floor and its "carapace of screens" is the primal scene, equally deploys intensive interviewing alongside participant observation as methods (Zaloom 2012 p171). Thus the pioneering study of "post-social relations in financial markets" was based on hundreds of interviews with traders (Knorr Cetina and Brugger 2000).

In this respect there is little innovative in methods in assemblage theory and sociology of finance, since elite interviews have long been a core method in economic geography (Cochrane 1998, McDowell 1998). My research approach to interviewing is conventional, emphasising semi-structured and open-ended elite interviews. There are however specific issues relating to qualitative research and elite interviews in Eastern Europe, which I took into account when designing a research strategy. Geographer Paul Richardson, having conducted 25 elite interviews in Russia for his PhD on Russian foreign policy, argues that "gaining access to elites can prove to be one of the most challenging aspects of the research process" (Richardson 2013 p182). According to Richardson, it is important to get the most of such hard-won individual interviews by triangulating them with other approaches (Richardson 2013). I took this into account through extensive triangulation of interviews with digital data research, as discussed below.

Alexander Kupatadze, researching oligarchs and organised crime in Ukraine, Kyrgyzstan and Georgia, conducted around 100 interviews in the course of his PhD compared to Richardson's 25 (Kupatadze 2012). He had previously researched the topic for three years for an NGO, pointing to the advantage for the researcher from having a pre-existing network. However, Kupatadze's approach to interviewing was more informal than Richardson's, which facilitated interviewing. He did not always fully disclose the nature of his research, and it was often not feasible for him to obtain informed consent in writing from participants. He also notes that despite stating his identity as university researcher, many interview participants believed him to be an undercover intelligence officer (Kupatadze 2012). Thus a larger number of respondents was gained by a more liberal approach to informed consent.

My interviewing strategy was midway between Richardson's and Kupatadze's approaches. I was always open about my research interest and identity, since I believe that the mere fact of interviewing elites does not permit the researcher to lower his or her own ethical standards (Morris 2009, Smith 2006). Again, I compensated for restrictions to interviewing on a sensitive topic by developing a parallel strategy for digital data.

Positionality, investigative journalism and academic ethics

Regarding positionality, and given my professional background as investigative journalist, I reflect here on the differences in practice and ethics between investigative journalism and qualitative social research. I have worked as a journalist in Eastern Europe and written about issues of illicit finance and money laundering including the Latvian banking sector. I continued to make occasional contributions as a journalist during the PhD. Therefore, I had some marginal role in developments analysed here. However, given that assemblage theory postulates that the researcher is always part of the network she or he is researching, and never has an exalted external view, this is only a strong version of the epistemological status of the researcher according to assemblage theory (Ruming 2012). My positionality was thus closer to Kupatadze's than Richardson's, given the former's previous experience of his research field in a non-academic capacity. While some interviewees may have been aware of my work as a journalist, I approached and engaged them as a University of Nottingham researcher, emphasising at all times that I was acting in an academic capacity. This also provided them extra guarantees of anonymity regarding use of their data.

While having a similar research field, the difference between qualitative social science enquiry and investigative journalism lies in the contrasting ethics regimes. The journalism ethics regime derives from the public sphere and its lead principles are freedom of speech and public benefit. The social science ethics regime has been adopted from biomedical research on human participants. Its lead principles are avoidance of harm to, and respect for privacy of, the human participants (Matheson 2019). Despite the broad similarities in what qualitative social science and investigative journalism research, these differences in ethical principles lead to a series of processual differences between the two professions. This applies to journalism's preference to name sources and clearly attribute information to them, in contrast to social science's insistence upon anonymity of participants. Informed consent and respect for privacy of research participants are principles of social science research that journalism largely respects, but may be waived where there is a demonstrable public interest ground for doing so - mostly regarding people in positions of power or influence (Chua 2020).

My personal experience in switching from journalism to social science was that the social science ethics code prompted deeper reflection on interviews. Journalistic practice thus could gain from academic ethical review by making the ethical decision-making process more reflexive. This has also been established in cases where journalism projects have been carried out by researchers at university journalism departments, and thus made subject to ethical review.

> Ethical review of a journalistic project can deepen its author's engagement with the power of journalism, and in particular the power of the privileged in reporting on others. In this kind of reporting, when journalism is consciously slowed down so as to disembed it from the moment of the news and so as to enable more explicit ethical knowledge (…) the university models some practices that the profession can draw from in daily work (Matheson 2019 p437).

At the same time as the academic ethics framework is enriching and reflective for journalists such as myself, there is also criticism of the biomedical ethical framework from within human geography. The core argument is that direct transfer of the medical ethics code to social science is misguided, since medical research ethics aim primarily to avoid the doctor/patient relationship conflicting with the researcher / research participant relationship. In social sciences, this conflict hardly exists, nor is there evidence that social science research has ever caused physical harm to participants (Dyer and Demeritt 2009, Atkinson 2009). As a result of stricter ethics review, sensitive or hidden research areas, where arguably the greatest need for research exists, may be left under-researched (Atkinson 2009). However, I argue that while ethics review can be restrictive on traditional fieldwork, this can be compensated by new research avenues that have opened up due to the availability of extensive digital data.

Progress of fieldwork

Ethics review and risk assessments for my fieldwork were made more complex due to a spate of killings of journalists, activists and investigators across Europe researching similar topics in 2016-2018, which raised the risk profile of research into money laundering, organized crime and corruption. This included the killing of journalist Pavlo Sheremet in Kyiv in 2016 (Guardian 2016); of Maltese investigative journalist Daphne Caruana Galizia in 2017 (Guardian 2017d); of Slovak investigative journalist Jan Kuciak and his partner in February 2018 (Guardian 2018b); of civil activist Kateryna Handziuk in Kherson, Ukraine, in November 2018 (NY Times 2018); and of Saudi journalist Jamal Khashoggi in Istanbul in October 2018 (BBC 2018c).

Directly impinging on my area of research, in May 2018, a Latvian professional bankruptcy administrator was shot dead in Riga in a contract-style killing in broad daylight. He had been reportedly lobbying in the US for the bank ABLV to be placed under external administration rather than self-liquidate, after the withdrawal of its licence in February 2018. No arrests have been made to date (Caruana Galizia 2019). The unpunished professional killing of a figure directly connected to my field of research raised apprehensions.

Furthermore, the Russian assassination attempt on former spy Viktor Skripal in Salisbury, UK, in March 2018 caused a further spike in tension between Russia and the West, which had already been running high since the Ukraine crisis of 2014, as did the ongoing investigation into alleged Russian interference in the US 2016 presidential election campaign (BBC 2019, BBC 2020). Adding to these tensions specific to the region were multiple arrests of academics conducting research overseas, in United Arab Emirates and Iran (Guardian 2018d, Guardian 2020a, RFE/RL 2019). These killings and arrests indicated a surge in repression of researchers and journalists outside of notorious hotspots such as Mexico, Syria and Afghanistan.

Due to the above-named factors in combination with the sensitive nature of the research topic, ethics review was protracted and approval came with the caveat that I should interview remotely rather than in-person, and concentrate on interviewing experts, regulators, investigators, journalists and former bankers, rather than discussing specific banking transactions with participant bankers. Because of the situation with Sars-Covid-2 in 2020, restrictions on in-person interviewing proved prescient, as most communication migrated online. However, it should be mentioned that the world-wide lockdown impeded interviewing because of the disruption it caused to work schedules. Closure of universities and libraries impeded researching and writing of the thesis, while combining home office with home schooling as a parent during lockdown was also challenging.

Saturation and sampling

The issue of saturation is central to the question of how many interviews is enough. As such, saturation was hard to achieve in this research. The reasons for this have already been discussed: Firstly the layers of secrecy surround the practices of offshore banking in Riga which make it hard to find interview partners on the inside willing to participate, a fact that other investigators have acknowledged (interview #1, Latvian investigative journalist). Another investigative journalist writes that:

> One former ABLV employee in Riga, who worked in the bank's compliance team for over a decade and before that was a Latvian police officer covering economic crime, replied to my request for information on the bank's liquidation by saying: "It [is] very interesting. But why should I tell you something? What is your offer?" Another, four years in compliance at ABLV in Riga, said: "Thanks for the offer. Any royalties involved?" (Caruana Galizia 2019)

Secondly, the turbulent events of 2018 connected to the sudden US-led closure of offshore banking in Latvia during my research (see Chapter 8) added a new dimension to the topic, extending the range of actors to include US officials and US foreign policy under the administration of Donald Trump. Fourthly, interviewing was disrupted by the worldwide lockdown in 2020.

Saturation itself is a contested notion. Analysis of the number of interviews cited in dissertations as achieving saturation shows an unusually high frequency of multiples of ten, suggesting that there is often in fact a target number for interviews (Mason 2010). The existence of minimum number of interviewees is an open secret, with the minimum number of respondents needed cited variously as 30-50 (Mason 2010). While due to the issues discussed above I cannot be sure I achieved saturation, the number of interviews I conducted, 30, is regarded as an acceptable number of interviews for a PhD project, and I triangulated the interview with other rich sets of digital data.

Table 6. Interviews conducted, grouped by sample

Nr.	*Journalists*	*Date of interview*
#1	Latvian investigative journalist	29 September 2019
#2	Editor of Latvian bank journal	05 October 2019
#13	European investigative journalist	13 December 2019
#15	Latvian investigative Journalist	17 December 2019
#17	UK investigative Journalist	18 December 2019
#21	Latvian publisher, journalist	24 February 2020
#27	Latvian broadcast journalist	22 October 2020
	Investigators	
#3	Former UN arms control expert	06 October 2019
#4	US expert on Baltic finance, academic	07 October 2019
#8	Former AML officer in US Bank	10 December 2019
#11	Investigator for Council of Europe	11 December 2019
#20	Former AML officer in European bank	13 February 2020
#22	UK anti-corruption financial investigator	26 February 2020
#25	Latvian anti-corruption NGO investigators	3 July 2020
#29	British AML officer	14 December 2020
#30	Former US law enforcement officer	18 December 2020
	Bankers	
#4	Former manager at Latvian bank	06 October 2019
#6	Former shareholder of Latvian bank	15 October 2019
#7	Former Ukrainian banker	21 October 2019
#10	Former bank AML officer, Latvian financial market official	11 December 2019
#23	Former Latvian bank manager	24 June 2020
#24	Former Latvian bank manager	2 July 2020
#26	UK academic	6 July 2020
#28	Ukrainian banker	31 October 2020
	Latvian regulators	
#9	Former adviser to Latvian prime minister	10 December 2019
#12	Former Latvian auditor at big 4 auditor	12 December 2019
#14	Former Latvian finance minister	16 December 2019
#15	Member of Latvian parliament	17 December 2019
#18	Former Latvian financial market regulator official	23 December 2019
#19	Former Latvian finance minister	10 January 2020

Regarding sampling, the 30 interviews were from around 50 interview candidates approached for their insight. I identified four groups with insight into Riga offshore banking. Apart from bankers themselves, these comprised regulators, journalists and professional investigators. Given the difficulties gaining access to bankers, this strategy also reflected advice for researchers of hard-to-access locations to "follow the trail of those mediators who have made it their task to name and open up worlds of secrecy," i.e. the investigators and whistleblowers who are "a part of the network that one studies" (Best et al 2013b p347). I also judged this sampling would achieve a balance between bankers, government regulators traditionally protective of the bank sector as argued below, journalists holding an overall neutral-critical position, and investigators professionally critical of the offshore banking sector.

Interviews took place against the background of an ongoing review process by Moneyval and OECD of Latvia's financial sector, with widespread apprehensions in Latvia that these organisations could greylist Latvia, which may have affected respondents' answers, as well as willingness to be interviewed. The final round of interviews took place in autumn 2020, after the publication of journalist investigations under the title 'FinCEN Files', comprising leaked suspicious activity reports filed to the US anti-money laundering office FinCEN, many of which detail transactions by Latvian banks (ICIJ 2020).

4.4 From the data desert to data deluge: Using open data in financial geography

This research project reflects one of the Economic and Social Research Council's priorities for 2016-2020 in "[e]xploring the potential of new forms of data (both quantitative and qualitative) (…) to support bold and innovative social science" (RCUK 2016 p15). Whereas there was previously a "data desert" pushing researchers to take risks both for themselves and for respondents in order to generate data on sensitive topics, now there is a digital "data deluge," tapping into which may enable researchers to obtain more robust research results than by traditional fieldwork while avoiding the ethical challenges associated with interviewing (Anderson 2008).

> To date, those in the knowledge business have been operating in data deserts, seeking to extract information and draw conclusions from a small numbers of observations. This is particularly the case in the social sciences and humanities, where studies might comprise a fairly small number of interviews or surveys, or a handful of

> ethnographies or case studies. (….) Big data holds the promise of a data deluge - of rich, detailed, interrelated, timely and low-cost data - that can provide much more sophisticated, wider scale, finer grained understandings of societies and the world we live in. (Kitchin 2013 p263)

Geographers, human rights activists and journalists working in the tradition of ‘open source intelligence’ (OSINT) have used open sources successfully in research, for instance to combat rights abuses. Geographers for instance have used satellite imagery to identify brick kilns in South Asia that are possible sites of slavery (Boyd et al 2018). One facet of OSINT research is ‘follow the money’ investigations, which draw on the trends towards open data on the part of governments. “[W]ell-structured and accessible databases can be goldmines for investigators and members of the public” (Radu 2016). Thus, according to a UNESCO primer for investigative journalism:

> Most of what we call “secrets” are simply facts that we haven’t paid attention to. Most of these facts - the usual estimate is about 90% -- are available for our perusal in an “open” source, meaning one that we can freely access (…) In the contemporary world, open sources are practically infinite (Hunter pp26-27)

While the current political situation and the longstanding overall risks inherent to the CIS countries mean that conducting fieldwork there is fraught with risk, the options for using big data and open sources for research into the former Soviet countries are broad, since Russia and Ukraine provide wide-ranging open access to large data sets. Both Russia and Ukraine, for instance, score well in rankings of open government data. According to the Open Barometer on data openness for 2018, Russia is at place 13 in the world and Ukraine on place 18 (World Wide Web Foundation 2018). This makes OSINT-type ‘follow the money’ research in the countries of the former Soviet Union a viable strategy.

In considering types of digital data that would be fruitful for researching offshore banking in Riga, I considered the topology of the internet. According to the International Encyclopedia of Geography, the Internet is regarded as comprising the ‘surface web’, the ‘deep web’, and the ‘dark web’ according to the form of access (Xu 2016). A fourth category I use which cuts across these three categories, is the social web, or use of the web as a means of direct person to person communication, where point of access is the smartphone. Table 7 shows these four categories.

Table 7. Topology of the Internet

Web topology	Definition
Surface web	Accessible by search engines such as google, bing etc because pages have links
Deep web	Comprises 90% of the web not accessible by search engines, such as proprietary databases ranging from library catalogues to email accounts and bank accounts.
Social web	Accessed mostly via smartphones, this category intersects surface and deep web, comprises user-generated and shared content, internet discussion forums, communication, chat groups, social networks,
Dark web	Accessed via TOR browser, anonymous, contains hacked data sets among others things

(Source: adapted from Xu 2016)

I sought data across each of these four categories in order to research Latvian offshore banking. Thereby for ethical and cybersafety reasons I regarded the 'dark web' as a category of data - leaked digital data sets - independent of the actual mode by which I accessed the data, which did not involve the dark web. For each of these categories of data, I sought traces left by the practices of Riga offshore banking. Each of these categories has its own specific structure and ethical requirements when extracting data, which I consider below. Following this, I will discuss the ethical considerations pertaining to the use of digital data.

Deep web

- investigations of economic crimes in Ukraine involving foreign banks as contained in Ukraine's online register of court decisions.

Surface web

- online profiling of Scottish Limited Partnership shell firms' business activities - as proxy for clients of Latvian banks - generated using a web scraper.

Social web

- contents of Russian-language chat forums (via an encrypted messaging app) of shell company incorporators and operators linked to Riga banks 2018-2019.

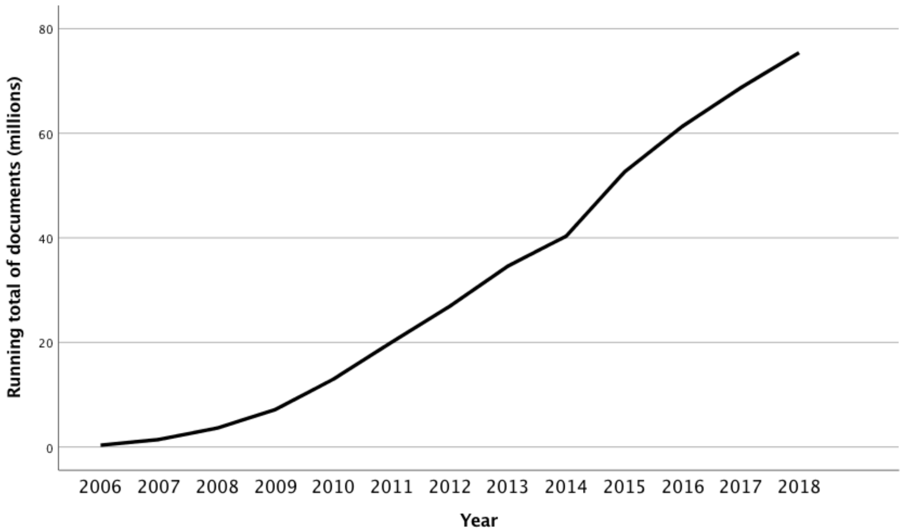
Dark web

- accounts of around 30 offshore firms banking via Baltic banks, used by 'black market operators' for making payments on behalf of clients, which comprise part of the informal institutionalisation of Latvia as an OFC (Fituni 2000, Ledeneva 2000).

Deep web

I will draw on the Ukraine's online unified state register of court decisions (USRCD), created in 2006. The register encompasses all court rulings of all types of courts. The USRCD redacts personal data of participants of court proceedings but retains names of legal entities, meaning that the database provides voluminous data on financial and commercial transactions. The search parameters allow for searches to range from broad keyword searches of the entire database using Boolean indicators, to searches for a specific court session by defining the court and date, the case number, the type of law (criminal, commercial, civil, and administrative), etc. Thus, the USRCD contains a comprehensive body of text data regarding Ukrainian political economy, all of which is accessible by keyword search. The current number of court documents in the system is now slightly over 70mn, with up to 30,000 new documents uploaded daily.

Figure 1. Number of documents uploaded to the USRCD per year.



(Source: USRCD)

Table 8. Number of documents in the USRCD by type

Type of court	Number of documents in the USRCD (27/1/2019)
Civil law	28,353,835
Administrative law	22,335,164
Criminal law	10,386,162
Administrative infractions	8,567,802
Commercial law	6,835,651

(Source: USRCD)

In this paper I canvass criminal law cases in the database to identify 213 investigations of economic crimes involving foreign banks 2007-2017. I analyse these along a number of trajectories to delineate the role played by Latvia's offshore financial centre in Ukraine's political economy.

Surface web: Scraping Scottish Limited Partnerships as a proxy for Riga-based offshore banks

One approach to analysing offshore banking in Latvia is to focus on the business profile of a legal form strongly linked to Riga offshore banks - the Scottish Limited Partnership (SLP). Legislated in 1907, this legal structure has experienced rapid proliferation since 2008 as a preferred vehicle for businesspeople moving dollar funds via Baltic banks, including Riga banks. Thus part of my methodology is to use Scottish Limited Partnerships as a proxy for the operations of offshore banking in Latvia. In this way, I aim to establish an overall business profile for clients of Riga offshore banks.

I ran a basic web scraper using a Microsoft Visual Basic script launching Internet Explorer out of Excel to run a search in DuckDuckGo, a web search machine that does not track searches. The web scraper produced a list of links referencing the name of the individual SLP, for each individual SLP, where links were available. I then manually coded each SLP according to the business profile derived from this assessment. This process required me to visit each link manually, thereby also verifying the legitimacy of the resource accessed.

Social web: Telegram chat groups

As one data source, I propose to analyse professional Russian-language chat groups for offshore banking, using discourse analysis (Glynos et al 2009). These chat groups emerged in 2018 in response to sweeping changes in the structure of the offshore banking market triggered broadly by anti-Russia sanctions implemented by the US. I will use the online discussions to research the following questions in particular:

1) How has the geography of the offshore banking market changed?
2) How has this impacted on Latvia as an offshore financial centre?
3) What does the future hold for offshore banking in general and Riga offshore banks in particular?

I identified three telegram ‘channels’ comprising users of Latvian offshore banks / offshore companies. The largest chat group comprises over 1000 members, with 150-200 on average online each day, generating around 50 posts per day. All three chat groups are in Russian. The total text corpus available currently is over 250,000 words. The rules of the largest channel are: “We aim for the chat to be professional and interesting. Here we exchange information, contacts, share our successes and problems. We observe the following rules: stay on topic, respect others, don’t flood or spam.”

Dark web

The data consists of US dollar accounts of around a dozen offshore firms banking at Baltic offshore banks about ten years ago, in the form of bank statements over 1-2 years. The bank statements contain details of incoming and outgoing payments, including originating or receiving entity, their respective bank account, size of payment, and purpose of payment. My approach is to map the flow of payments through these offshores accounts, as proxy for the financial flows through the Baltic offshore banks. I am not interested in any specific transactions, but in aggregating the financial flows between jurisdictions.

Ethics of digital research

When researching ethically challenging topics such as money laundering, digital approaches reduce many of the ethical issues that arise when directly involving human participants through interviewing. However, ethical issues regarding privacy and consent do arise from fast evolving digital research strategies. The Economic and Social Research Council recognises this state of flux in “a fast developing area” in its latest 2015 update of its ‘Framework for Research Ethics.’

> [W]hat constitutes ‘privacy’ in an online environment? How easy is it to get informed consent from the participants in the community being researched? What does informed consent entail in that context? How certain is the researcher that they can establish the ‘real’ identity of the participants? When is deception or covert observation justifiable? How are issues of identifiabilty addressed? (ESRC 2015)

Due to the fast-changing situation, there is consensus only that in digital data there is no polarity existing between public and private, but rather a spectrum running from the public to the private. According to the latest report of the Association of Internet Researchers (AoIR), which aims to set a benchmark for best practice standards for online research, the current situation is that “[s]ocial, academic, or regulatory delineations of public and private as a clearly recognizable binary no longer holds in everyday practice.” (Markham and Buchanan 2012).

Given the fast-changing reality of digital research, current ethics guidelines for this area acknowledge they are work in progress. “[N]o set of Internet research guidelines can be static, because technologies and the way that technologies are used are constantly changing” (Townsend and Wallace 2016 p15). Most recent accounts of the ethics of research therefore argue that such issues have to settled on a case-by-case basis (British Psychology Society 2017). According to a recently published manual for online social science research, a key part of this process of moving towards formulating clear rules in the future is that researchers in the present be explicit about the decisions they make to spur on debate (Eynon et al 2016).

Practice is arguably moving ahead fast than the ethics framework. Thus, regarding the consent of research participants, a survey of articles based on British parenting site Mumsnet shows that in practice consent is often not requested from digital contributors who have posted to an open forum using an avatar. I identified over 100 peer-reviewed articles based on online user content posted to Mumsnet since 2007, almost all of which related to issues of personal sensitivity, encompassing personal hygiene, mental health, domestic violence and personal debt. Most investigators did not solicit consent from the Mumsnet contributors given that the Mumsnet online discussion forums are publicly accessible, and contributors use avatars.

Regarding the use of informally obtained data, human geography has been a pioneer in using leaked data for research purposes in contexts where the public interest was judged to outweigh the illegal origins of the data. 'Eurasian Geography and Economics' was one of the first periodicals to publish research based on the Wikileaks cache of leaked US diplomatic cables (O'Loughlin et al 2010). A 'Progress in Human Geography' review assessed the article as a pioneering attempt to combine quantitative with qualitative approaches (Sui and DeLyser 2012). Wikileaks is on one hand an extreme case because of the classified status of the data as decreed by a great power. On the other hand, Wikileaks has become 'the new normal' following a succession of similar scale leaks such as 'Snowden Papers' and 'Panama Papers' driving on global affairs and indeed supporting the progressive agenda on surveillance and tax evasion. "Mass leaks, on a scale inconceivable back in the paper-only era, have become so routine globally that only the most extraordinary get extended attention" (New York Times 2019). The data I use, leaked legacy bank transaction data of defunct banks, is itself used by law enforcement agencies across Europe to trace laundered funds (OCCRP 2019a).

My ethics strategy across the surface, deep, social and dark webs is to redact all personal information and any discussion of specific transactions, from digital data thus to treat the data as "an aggregate which draws attention to prevailing themes, rather than attending to the practices of any individual use" (Hine 2014 p576). This includes also masking the original locus of quotes and any cited transaction data.

4.5. Conclusion

This chapter has outlined my dissertation's research question, design, methodology and ethical considerations. I use a qualitative case study of Latvia's financial sector 1992-2018 to explore how the FATF regime impacts on illicit offshore flows. Latvia was chosen because of its banking sector activities in the 1990s handling dirty dollars from Russia and other former

Soviet countries. Its subsequent rapid implementation of AML and integration into NATO, EU and Eurozone make it a suitable case to examine the impact of the FATF regime on illicit offshore finance. The topic of money laundering presents difficulties to the researcher because of the ethics and safety issues arising in connection with fieldwork. I negotiated these difficulties with a strategy of remote interviewing combined with a digital data strategy gleaning data from the surface web, deep web, social web and dark web. In doing so, I was mindful of ethical issues of privacy and consent. Despite challenging conditions in the field, it was possible to acquire sufficient data to answer the research questions. The next chapter tackles the first of these questions in the emergence of offshore banking sector in Latvia in the 1990s.

Chapter 5. The emergence of offshore banking in Latvia in the 1990s

5.1 Introduction

This chapter explains how offshore banking - understood as banking services offered to non-residents in foreign currencies - emerged in Riga in the process of Latvia's disentanglement from the Soviet Union, and what financial operations it involved. The offshore sector emerged partly from the ill-fated attempt to introduce market mechanisms to the Soviet Union and partly from Latvia's attempt to re-establish its independence out of the ruins of the Soviet Union. These vectors created a cluster of banks in Riga acting as the entry point to the accelerating global financial system, in particular the US correspondent banking network, for secretive, shadow-economy money from the CIS countries.

This chapter is organised into three sections. In the first section, I deal with the emergence of commercial banks during the final years of the Soviet Union, and how these local banks meshed with US correspondent banking following the collapse of the Soviet Union. In the second section, I show how the political economy of newly independent Latvia interacted with the rise of a dynamic local banking sector based on money from the other former Soviet countries. In the third section, I describe how this new offshore banking sector in Latvia mediated between US correspondent banking and the post-Soviet shadow economy. Riga therefore started to operate as a financial centre, in the sense of acting as "a bridge, an intermediate space between the globalised part of finance and the thick national and local cultures of investment of a country or a region" (Sassen 2012).

5.2 From Soviet to SWIFT: Banking and the collapse of the Soviet Union

The emergence of commercial banks across the Soviet space was not just a consequence of the collapse of the Soviet Union. Rather the introduction to the Soviet Union of commercial banking in the late 1980s, as part of the Perestroika economic reform program launched in 1985, played a key, if unintended, role both in bringing about the demise of the Soviet plan economy, as well as determining what came after. This was for two main reasons. Firstly, the introduction of commercial banks across the Soviet Union provided one of the channels for officials to privatise state assets, eventually causing the implosion of state structures, and the subsequent collapse of the Soviet Union, as elites grabbed as much as they could and ran for the exit (Solnick 1998). Secondly, as Latvia wrested independence from Moscow, the newly emerged commercial banks in Latvia created a channel to convert privatised ruble assets into dollars and move them through the international financial system.

The introduction of commercial banks proved unintentionally disastrous for the Soviet Union because the Soviet plan system was based on the strict separation of cash money, used almost exclusively for wage payments and household purchases, from non-cash ledger money, used as an accounting unit in the centralised planning system. (Handelman 1995 p136, IMF and World Bank 1991). In a planned economy organised vertically, there was no need for money as a medium of exchange outside the day-to-day consumption of households. If an enterprise wanted to boost its liquidity, for instance, it could not accumulate cash, but might instead horde inventory to protect against anticipated future shortages (IMF and World Bank 1991). But during Perestroika the Soviet authorities tried to liberalise the economy by giving enterprises more autonomy and by permitting new forms of entrepreneurial activity, starting with the 1987 Law on State Enterprises. Companies started to use money as a resource, rather than just for accounting. Money held by companies thus became more liquid and fungible, acquiring more of what an IMF report on Soviet banks referred to as ‘moneyness’, rather than being a mere accounting tool (IMF and World Bank 1991). This weakened the previously rigid separation of non-cash ledger money from cash.

At the same time, the May 1988 Law on Cooperatives allowed the establishment of cooperatives operating under the umbrella of large state enterprises, but which would be organisationally and legally separate, operating outside of the planned economy to produce goods directly for consumers (Solnick 1998). The law also allowed the establishment of cooperative banks. In September 1988, state enterprises were allowed to directly create their own commercial banks (IMF and World Bank 1991). These reforms failed to produce the desired surge in productivity, but they did trigger the mass founding of banks across the Soviet Union, with over 400 commercial and cooperative banks having been founded by September 1990 (Johnson 2000).

There was almost no prudential supervision in place for these new banks because commercial banks had not previously existed in the Soviet economy. The new licences allowed banks a full range of operations, including long- and short-term lending and accepting deposits from any enterprises and households (Solnick 1998, IMF and World Bank 1991). As a result, a private and largely unsupervised banking sector appeared in the Soviet Union early in the liberalisation process, while almost the entire remaining economy remained in state ownership and governed by state planners. “By condoning the creation of barely regulated cooperative and commercial banks, Gorbachev’s government unwittingly liberalised the new Soviet financial system early on in the reform process” (Johnson 2000 p34). Policymakers’ aim was to dynamise the failing Soviet economy by introducing capitalist elements, but creating commercial banks at the same time as giving companies more financial autonomy had the opposite effect; that is it accelerated the collapse of the Soviet economy (Solnick 1998).

The nascent private banking sector in combination with the increased ‘moneyness’ of state enterprise finances created a channel by which Soviet functionaries could gain personal control over cash flows in the Soviet economy. Of 64 new commercial banks, over half had been created by USSR ministries, regional Soviets or Communist Party organisations (Johnson 2000). Gorbachev commented regarding these reforms that “a channel was formed for converting noncash money into cash” and, according to Johnson, “[i]t soon became clear that the CPSU [Communist Party of the Soviet Union] regularly ‘privatised’ its resources through the emerging banking system” (2000 p36). This was the birth of the massive post-Soviet shadow economy still existing today. I define shadow economy here as “all economic activities which are hidden from official authorities for monetary, regulatory, and institutional reasons” (Medina and Schneider 2018 p4). Thus I use the term ‘shadow economy’ entirely in the traditional use deriving from economics and economic sociology, synonymous with the term ‘underground economy’ (Portes and Haller 2010). While recently academics have focused attention on ‘shadow banking’ as denoting new and hidden forms of lending (Nesvetailova 2015, 2017), I use the ‘shadow’ metaphor purely in the former, traditional sense, referring to the totality of unreported, unrecorded, informal and /or illegal economic activity (Portes and Haller 2010). This being said, for the reasons explained above, the post-Soviet shadow economy and the sprawling post-Soviet commercial banking sector, comprising over 1000 banks in Russia alone, were from their origins in late Perestroika onwards closely intertwined.

The global expansion of transaction business in the 1970s and 1980s

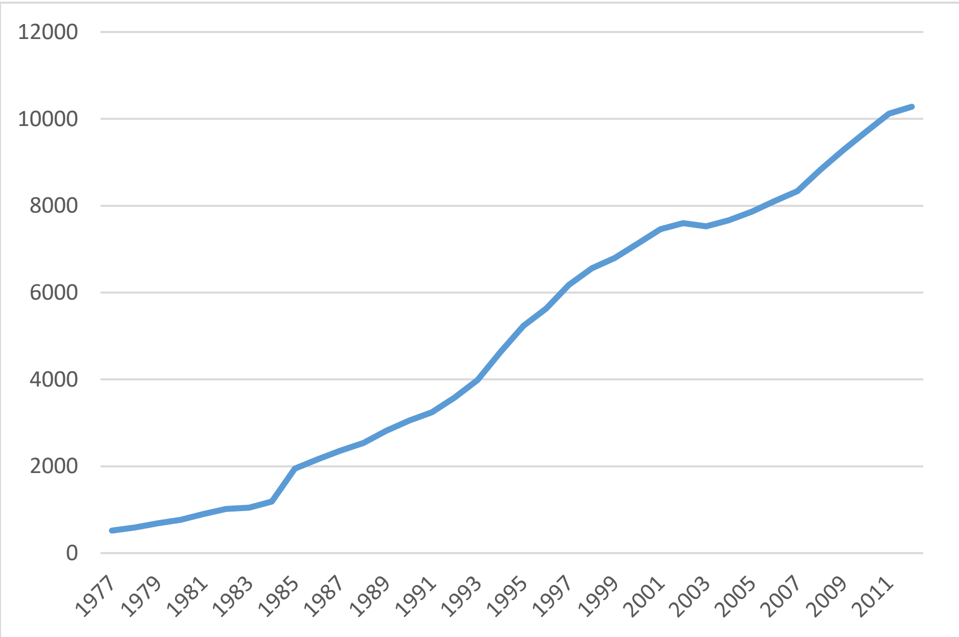
In this section I will discuss how one overlooked aspect of financial globalisation meshed with the embryonic banking system that emerged across the former Soviet countries in the early 1990s. This financial globalisation process was the rapid expansion in international payments business in the 1980s. The expansion of global payments, in banking parlance 'transaction business', was one of the underpinnings of the globalisation of financial markets gathering pace in the 1980s. However, because bank payments systems are often regarded as mere "financial plumbing," this expansion and its subsequent impact on the post-Soviet countries in the 1990s, has been little remarked upon (Scott and Zachariadis 2014 p2).

As the result of the acceleration and expansion of international payment traffic, by means of new telecommunication technologies interacting with increased demand for international payments, international payments metamorphosed from being an additional service offered by banks to clients of their lending business, into 'transaction business', an important high-volume profit-driven business in its own right (Langdale 1985). In the 1990s, the crisis-wracked post-Soviet economies offered little lending business of interest to global banks but did offer a potentially profitable market for their global transaction business in the embryonic post-Soviet banking system. If the emergence of commercial banking in the late Soviet Union had created a channel for the "conversion of non-cash funds to cash" as described, the meshing of these post-Soviet banks with the expanding globalised transaction business created a channel for this cash to flow out of the former Soviet space into global financial centres.

The core of "financial plumbing" is the global network of correspondent banking, which enables any one bank to transfer a client's money across the world to accounts at banks in countries where it has no physical presence. The correspondent banking network comprises a mesh of bilateral relations between pairs of banks, with one bank, the *correspondent bank*, providing financial services, such as holding a deposit, for the other bank, the *respondent bank*. Major international banks, often US-based, may have thousands of respondent banks as clients, thereby providing the infrastructural backbone for global wire transfers.

Correspondent banking is one of the oldest branches of banking, going back to 14th century Venice (Norman et al 2011). In the 1970s, faced with the need to support ever intensifying global trade, the handful of transnational, mostly US-based banks, acting as 'money centers' in the system, had driven on its modernization, both cooperating and competing to introduce new telecoms technologies to accelerate payments (FinCEN 2006, Langford 1985). One of the major results of such collaboration was the Society for Worldwide Interbank Financial Telecommunication (SWIFT) bank messaging system. Established in 1973, SWIFT revolutionized the international funds transfer market via correspondent banking by introducing a global standardized messaging system that, as the acronym implies, hugely accelerated the international payments process. SWIFT become an engine for expanding international payments via banks, and thus for the "industrialization of financial services" (Scott and Zachariadis 2014 p2).   At the same time, "powerful private financial institutions own and govern SWIFT and clearly bias its governance towards the heaviest users of the network" (Dörry et al 2018).

Figure 2. Number of firms in the SWIFT system 1977-2011



Source: Scott and Zachariadis 2014, p113

SWIFT does not disclose information on payments. However authoritative sources put average daily transactions in 2005 at nearly $5 trillion worldwide each day, and average daily transactions in 2011 at $ 7.7 trillion per day (FinCEN 2006 p62, Scott and Zachariadis 2014 p95).

In parallel to the adoption and expansion of SWIFT, major transnational banks also developed their own inhouse technologies allowing clients to make cross-border funds transfers via the SWIFT system from their own terminals. Bank of New York (BoNY) in particular was recognised as having a market-leading technology, namely the micro/cA$h (sic) register computer-based software, which enabled clients to make international transfers round the clock, independent of bank supervision. In 1994, BoNY earned $530mn in payment processing fees worldwide, increasing to $1bn in 1997 (Block and Weaver p162). Competitor banks developed similar services.

The global transaction business and post-Soviet banking in the 1990s

While the crisis-ridden post-Soviet economies offered little lending business for global banks, they did see the rapid expansion in global banks' provision of correspondent banking services, facilitated by SWIFT. By 1995, seven major US banks reported having correspondent relationships with between 50 and 300 Russian banks each, in a country where commercial banking had not existed eight years previously (US Senate 2001). BoNY opened correspondent accounts for 52 Russian banks in 1992, the first year of Russia's independence, and by 1994 had opened correspondent accounts for 355 Russian banks, many of which were tiny banks created from scratch (Block and Weaver p106). Deutsche Bank USA opened 149, while HSBC Bank USA opened 283 correspondent accounts before 1998 (US Senate 2001).

This rapid and largely undiscriminating expansion of correspondent banking service to myriad new banks attests to transaction business' drive to maximise financial flows:

> Transaction service banking is a volume game. You earn very little per transaction. So you need to you need to create systems that allow you to process as much as much volume as possible and as cheaply as possible so you can attract as much money as possible. And so if you're in a country or you're in a region, then you want to be competing for as much of that business as possible (interview #26, UK academic)

The spread of US correspondent banking services across the post-Soviet space took place simultaneously with an economic collapse widely described as the greatest peacetime economic collapse ever recorded, combined with widespread breakdown in law and order (Stiglitz 2002). Large-scale capital flight ensued. There is ongoing debate about the size of capital flight, both legal and illegal (Novokmet et al 2017). The US State Department's 1999 International Narcotics Control Strategy Report cited a claim by the Central Bank of Russia that $78 billion had been illegally sent out of Russia to offshore accounts in 1998 alone via correspondent banking (BINLEA 1999).

Given the weakness of the newly formed post-Soviet states set against the Soviet legacy of complete state ownership and economic control, vast assets distributed across the entirety of the Soviet Union were effectively rendered ownerless by the Soviet collapse. Furthermore, as described, the local commercial banking sector had emerged largely as a channel to "convert non-cash money into cash". With the arrival of US correspondent banks, these banks were then hooked up to the high-volume global transaction system, facilitating the outflow of funds from the former Soviet countries.

The ready availability of these new high-speed international correspondent banking relations drove on the development of the banking system across the post-Soviet countries. Accessing international correspondent banking services became the main activity of many new banks, as analysed by a US Senate investigation on abuse of US correspondent banking:

> These high-risk foreign banks typically have limited resources and staff, and they use their correspondent bank accounts to conduct operations, provide client services, and move funds. Many of the banks reviewed by the subcommittee deposit all of their funds in, and complete virtually all transactions through, their correspondent accounts, making correspondent banking integral to their operations (BINLEA 1999).

The transaction pattern provided further strong indication that this was money-laundering activity, namely the apparent redundancy of many of the wire payments:

> (…) In many instances, the activity seems to have no purpose other than to move a transaction through a series of financial institutions, domestically and internationally. Such activity may reflect what law enforcement officials call "layering," or the transfer of funds to and from various locations and accounts for the express purpose of concealing the nature, origin or beneficiaries of the transactions. (BINLEA 1999)

In 1999, a small subsection of these activities connected to Russian correspondent accounts at US banks were highlighted in a major international scandal, and a US domestic political controversy, connected to the Bank of New York (BoNY). The Bank of New York scandal hit US headlines, with media reports of $7 billion in suspect funds moving from two Russian banks through a U.S. bank to thousands of bank accounts throughout the world. In 2001 two mid-ranking BoNY offices pled guilty to money laundering designed to "help Russian individuals and businesses transfer funds in violation of Russian currency controls, customs duties and taxes" (US Senate p644). Some of the $7bn may have been funds lent to Russia by the International Monetary Fund and some connected to post-Soviet mobster Semen Mogilevich. The $7bn was then paid out in over 160,000 wire transfers to hundreds of beneficiaries, mostly shell firms, across the world (US Senate).

Later courtroom disclosures shed more light on BoNY's overall modus operandi via its correspondent banking activities in Russia, of which the episode highlighted in media was only a small part. A lawsuit bought by BoNY shareholders against BoNY in 2002 deriving from the BoNY scandal detailed how, in 1992, Bank of New York, one of the largest providers of correspondent banking services worldwide, had created a new Eastern European division to market its correspondent banking services across the territory of the former Soviet Union. BoNY staffed the department with Russian speakers from the US-Russian diaspora. (BoNY Litigation 2000, Block and Weaver 2005, Kochan 2005).

The new department marketed BoNY's correspondent banking business to the new banks appearing across Russia and former Soviet states According to the lawsuit, BoNY actively promoted use of these correspondent relationships for post-Soviet bankers to transfer funds out of Russia as fast as possible with no questions asked as to the origins of those funds. BoNY's Eastern European division devised mechanisms for moving billions of dollars, while concealing its movement. Together with Russian bankers, BoNY devised a scheme called in Russian '*prokrutki*', meaning spinning, designed to hide the path of money by 'spinning' it through several layers of shell companies (BoNY Litigation 2000, Block and Weaver 2005, Kochan 2005). The second component was what BoNY officers called in Russian '*konformashka*' - a slang word denoting the forging of documentation to make fund transfers seem to conform to a genuine business transaction, such as export contracts, consulting services or loan agreements. Furthermore, according to the complaint, BoNY officers marketed to Russian bankers what they called a "global custody system" comprising a network of hundreds of offshore shell firms in jurisdictions across the world, through which money would percolate. BoNY would then design such a "global custody system" for each Russian bank designed to help bank customers avoid tax, but also to help criminal money be moved internationally undetected (BoNY Litigation 2000, Block and Weaver 2005, Kochan 2005). BoNY's micro/ca$h register system played a crucial role in implementing this business (*Non-prosecution agreement*…).

As I will argue in Chapter 7, this scheme of '*prokrutki* / spinning', '*konformashka* / forged documentation' and 'global custody system' corresponds to what investigative journalists have latterly referred to as 'laundromats,' referring to money laundering via Baltic offshore banks and US correspondent accounts. From the CIS perspective, these arrangements in combination with networks of locally organised shell firms are known as a 'platform' (interview #13 European investigative journalist, interview #7 former Ukrainian banker). Thus, it appears to have been a general scheme implemented across US correspondent accounts when globalised transaction banking meshed with the post-Soviet shadow economy. Given state weakness at the time, this amounted to the integration of the huge post-Soviet shadow economy into the global payment network via US correspondent banking services, i.e. the mobilization of the undeclared assets of the post-Soviet shadow economies for and by global capitalism via US correspondent banking (Palan 2009).

5.3 The political economy of offshore banking in independent Latvia

In this section, I examine the political economy of the banking sector in Latvia as it emerged in the 1990s out of the rubble of the Soviet Union, tracing the mutual relationship between the emerging banking sector and the politics of the newly independent Latvia. I explain the paradox of why Latvia - the overriding aim of which was to consolidate its newly found independence from the Soviet Union / Russia - nevertheless opened its new banking sector to money from Russia and the other former Soviet countries.

The discussion here is informed by topics that emerged in the literature review in Chapter 2 on the political economy of offshore finance. Hampton and Christensen's argument that the development of offshore financial centres results from capture of the local jurisdiction by representatives of financial capital is particularly fruitful in the post-Soviet context in Latvia

(Hampton and Christensen 2002). I will argue that in Latvia there was an alliance between financial capital and political forces looking to consolidate Latvia's monetary and political independence from Russia by instrumentalising Russian money.

The foundation for Latvia's path towards becoming an offshore financial centre was laid in the closing days of the Soviet Union, as commercial banks proliferated. In the Baltic republics, the intertwined dynamics of communist decline, banking liberalization and commercialisation were further caught up in the dynamics of the national liberation movements at the margins of the former Soviet Union (Lieven 1994, Auers 2015, Ducmane 1995). The Baltic states' drive towards monetary independence from the Soviet Union began even before the putsch attempt of August 1991 and saw preparations for Latvian banks to provide an additional service that was not yet readily available in the Soviet Union - the conversion of privatised resources into dollars.

Latvia's independence movement started preparing for monetary independence even before the pro-independence movement 'People's Front' won elections to the Latvian Supreme Soviet in March 18 1990, leading up to the Soviet's declaration of restoration of Latvian independence in May 4 1990. On March 2, 1990, Latvia's Supreme Soviet passed a law, "On Banks", which established - or restored - the pre-war Bank of Latvia as central bank, albeit initially in an embryonic form with a skeleton staff and few powers. Planning started immediately for monetary reform based on introducing free convertibility of the currency together with the creation of foreign exchange reserves, as part of a strategy of "currency substitution" towards the Soviet ruble (Vīksniņš 2008 p114). In November 1990, the Latvian Supreme Soviet legislated for the liberalisation of currency trading, which entered into effect on January 1 1991 (Ducmane 1995). This law largely abolished state regulation of foreign currency exchange in Latvia. Yury Yaremenko, a leading Soviet economist and adviser to Mikhail Gorbachev, referred to this development as "a death knell for the Soviet Union" because it allowed for the free conversion of rubles into foreign currency - US dollars - and thus the possibility to move money out of the country (Lapsa 2008). A subsequent Latvian prime minister, Māris Gailis, at the time head of the country's Department of External Economic Affairs, recalled the significance of the event in his memoirs:

> So in this way we went straight to market relations in one of the most important spheres - currency trading. It is worth remembering that there are not that many countries without restrictions on currency trading. Latvia is one of them, Israel for instance not. (Gailis 1997 p32)

Respondents also noted the full liberalization of currency trading as one of the key measures stimulating the dollarization of the financial sector and the development of offshore banking (interview #23, former Latvian bank manager). It still took three months for the Bank of Latvia to award what was the first licence for foreign currency trading on the territory of the Soviet Union, to a firm called Parex in March 1991 (Kommersant Den'gi 1996). One direct result of this early liberalisation of currency trading was the rise of the Parex financial group that played a key role in developing offshore banking in Riga. Parex was operated by two former officials from the Communist Party-affiliated youth organisation Komsomol, Valērijs Kargins and Viktor Krasovickis. In an interview some years later, Kargins hinted that Parex had pressured the embryonic Bank of Latvia into awarding the licence:

> We started changing money at the start of the 1990s … according to the principle that everything not forbidden is allowed. We decided to expand currency exchange operations only when backed by the law. At that time the Bank of Latvia had already been formed, as a national bank independent of the USSR: three men sat in one room - the president, an aide and a lawyer … We drew up the licence jointly with them, and tried to get them to sign. But they did not want to sign … To cut a long story short, they signed." (Kommersant Den'gi 1996)

This story exemplifies how Latvia's drive towards statehood and the development of offshore banking reinforced each other, partly because it was hoped that introducing the dollar to compete with the ruble would reduce Latvia's monetary dependence on the Soviet Union (Vīksniņš 2008). The Parex currency exchange business quickly grew, catering to the entire Soviet Union from out of Riga offices. It was one of the few points, if not the only point, where dollars could be bought for rubles legally in the whole Soviet Union:

> I remember how a plane flew in from Kazakhstan with the well-known, inexhaustible and omnipotent LB [name redacted in original] from Almaty, and the entire road from the airport to our office was lined with soldiers in uniforms carrying automatic weapons. Our armoured cars with money drove the road and the southerners looked around curiously at the unknown city. The process took on such a scale that sometimes we sometimes dispatched in one week several TU-134s [Soviet mid-range aircraft] stuffed with money into the Russian regions - in Orenburg, Siberia, elsewhere. We loaded the cash into the cabins, and the plane took off with the guards, cashiers and often with the owners of the money. (Kargins 2005 p122)

According to Kargins' account, Parex remained the only currency exchange organisation in the Soviet Union for another six months, until after the 1991 failed August putsch attempt, when other banks started currency trading in Riga. Moscow's emergent business press cited the Parex exchange rate as the quasi market ruble-dollar exchange rate. By July 1992, after Parex gained a full banking licence, it had a monthly turnover of over $20mn - a significant sum at that time (Lieven 1994).

As noted by Hampton and Christensen for Jersey, banks in Latvia were able to write much of the banking legislation themselves, a sign of partial state capture (Hampton and Christensen 2002). Parex from the start helped shape the institutional framework for banking in the newly independent Latvia, directly writing draft bills and regulatory instructions for the banking sector that were then adopted (Kommersant Den'gi 1996). Kargins called Parex simply "a state-supporting institution" which held significantly more dollars than the Latvian state itself (Lieven 1994 p364). The 1994 Parex annual report also noted the bank's direct input into financial sector legislation (Parex 1994). Kargins' memoirs claim he was one of the forces behind the creation of the political party Latvia's Way in 1993, which provided five prime ministers in the 1993-2003 (Kargins 2005). As a result Latvia's financial sector regulation was highly favourable for the development of dollar-denominated offshore banking.

Post-Soviet transit trade via Latvia, criminal involvement and the development of the Latvian banking sector

In the immediate post-independence years, banks proliferated in Latvia like "mushrooms after rain" [interview #19, former Latvian finance minister]. The first two banks in Latvia were found in 1988, by 1991 there were 16 and in the first two years of independence the number jumped to 61 in 1993, before dropping back down to 32 in 1996 (Association of Latvian Commercial Banks 1997). Latvia's fledgling bank sector's rapid growth was driven in the first part of the 1990s by the role played by Latvia as a transit route for exports of raw materials from Russia to world markets and, in particular, oil. The reason for the key role played by Latvia in Russian oil exports was the major oil transhipment terminal built at the port of Ventspils in Latvia in the 1960s. As late as 2001, around 21% of Russian maritime crude exports via ports passed through Ventspils, and income from transit from Russia still comprised 10% of Latvian GDP (Brodin 2003). It was not until 2003, when a new oil terminal was opened on the Russian Baltic coast at Primorsk that the significance of Latvia for Russian maritime oil exports dropped.

Following independence, the banking business started to provide short-term trade financing at over 100% interest rates for transit deals, which remained highly profitable while prices of oil and metals and other commodities across the former Soviet Union remained many times lower than world market prices (Fleming et al 1996). So profitable was the business, and so lax the regulatory framework for banks, that by 1994 there were a total of 56 banks which had doubled their assets from 1993 to 1994, although total assets at 1bn lats (around $2bn) were tiny compared internationally (Bank of Latvia 1994). International observers found Riga to be a "bustling financial centre (…) bridging east and west" (Euromoney 1994). But there was a dark side to this boom. Much of the transit flow via Latvia was involved in contraband schemes to avoid tax and customs payments in Russia, so that the "bulk of Russian contraband in raw materials and metals passed through Latvia Estonia and Lithuania" (Handelman 1995 p243-244). The transit trade was highly corrupt (Brodin 2003). Not surprisingly, the financial sphere that sprung up to service the flow was also highly criminalised.

As the Latvian economy stabilised, banks run by individuals with organised crime connections started to target the population's savings by offering high interest rates in what was ultimately a pyramid scheme, at the centre of which was the aforementioned Bank Baltija. By 1995, Bank Baltija, had over 120,000 depositors (around 5% of the population) who held around 100mn lats (around $200mn) in deposits at the bank (Delfi 2015). The Bank of Latvia belatedly intervened at Bank Baltija and discovered thereby that much of its funds had been siphoned off abroad. Since there was no deposit insurance at the time, a significant part of the population lost their savings. It transpired that the owners and managers of Bank Baltija had a criminal past, having served long sentences in Soviet times for economic crimes, and had ties to organized crime groups (FIU 2018). They received prison sentences. The level of gangsterism in Latvia in the 1990s may not have reach the level in the CIS countries, but was still significant.

> There was obviously a lot of criminal activity behind some of these banks. In one case, I remember we took a decision to close a bank and we were told by the CEO (…) that if we closed the bank, there would be people killed by the weekend. And sure enough, there was a shootout and people were killed. (Interview #23, former Latvian bank manager)

Bank Baltija was only the largest example of fraudulent bankers stealing depositors' money. In 1994-1995, Bank of Latvia withdrew the licences of 22 banks in connection with the banking crisis and tightening regulations. Gradually in the second half of the 1990s, locally owned banks were pushed away from working with depositors' money, as the state savings bank Unicombank was prepared for sale to Scandinavian banking groups (interview #24 former Latvian bank manager). In 1996, in the wake of the 1995 bank crisis, non-resident deposits exceeded resident deposits for the first time, according to the Association of Latvian Commercial Banks (Kommersant 1996). Offshore banks were segregated from the local retail market, but the legacy of fraud and organized crime continued to dog the sector.

Monetary independence, democracy and offshore banking

In the account above, the origins of offshore banking in Latvia show a number of similarities with Warf's account of the origins of offshore banking in Panama outlined in Chapter 2, in particular the role of transit trade prompting the emergence of a home-grown dollarized banking sector, and the small country having strategic significance for the US military (Warf 2002). One other parallel was that in Latvia as in Panama, offshore banking was supported by officials in sway to the Chicago school of monetarist economics. In Panama, the creation of an offshore financial centre in the 1970s was the brainchild of Panama's Minister of Planning, Dr Nicholas Ardito Barletta, who had studied in Chicago alongside Milton Friedman and was a convinced free marketeer (Warf 2002). In Latvia, central banker Einars Repše played a similar role. Repše, who became Chairman of Bank of Latvia in 1991 and quickly moved to introduce a Latvian currency independent of the ruble, was the dominant figure in Latvia's finances and macroeconomic policy in the 1990s (Vīksniņš 2008). He offered a clear monetarist vision and independence from Latvia's turbulent party politics afforded him by his position as central bank head. The International Monetary Fund's official history describes Repše as "a thirty year old physics graduate who had taught himself economics by reading Paul Samuelson's elementary text book (…) With the conviction of the revolutionary Repše decided that this was all the economics he needed to convert Latvia into a western monetary system" (Boughton 2003 p136).

The core of Repše's macroeconomic policy was maintaining the fixed exchange rate for the newly introduced Lat despite massive economic adversity, as part of the IMF's anti-inflation orthodoxy that saw "a strong link between fixed exchange rates and low inflation" (IMF 1996). According to the IMF, "the gamble paid off" for three reasons: the government maintained strict fiscal discipline similar to that imposed by a currency board, raised taxes successfully, while Western governments returned gold owned by the pre-war independent Latvia (Boughton 2003). But an additional factor was the transit trade and offshore banking sector growing up around it, which the Bank of Latvia strongly supported. Repše was one of the architects of offshore banking in Latvia, which flanked his monetarist policies:

> In the 1990s, Prime ministers and finance ministers were replaced almost every year, while Repše stayed put. Moreover, he had stronger views and principles than all the ministers. His economic ideas were clear and firm. He was a monetarist, who believed in a conservative monetary policy leading to stable prices, and he believed in an open economy. His ideal was Switzerland, and he desired that Latvia would develop into an international banking paradise characterized by the rule of law and monetary stability. (Aslund 2018).

Other observers at the time described Repše as being on the "radical-nationalist side of politics" which in monetary terms translated into support for early introduction of a strong stable Lat (Lieven 1994 p360, Vīksniņš 2008). Given Latvia's lack of export potential, the large flows of money in the newly emergent sector proved a key resource supporting the new currency, Repše argued:

> When we created the banking system, we intended for Russia to transport through our ports a significant portion of commodity exports. (…) In this case, we took into account our need for currency (…) We wanted money to flow here. Therefore, our banking laws were very liberal - no prohibitions on export or import. (…) Distances were also taken into account (to such banking centers as Switzerland and Luxembourg), the absence of a language barrier, the presence of a pure human connections, etc. This objective situation created a tangible influx of capital (…) Although it follows from the balance of payments that imports to Latvia exceed exports, the capital account (...) has remained positive, supporting the Lat. (Belorusskaya Delovaya Gazeta 1995)

Nearly twenty years later, Latvia's new financial sector regulator Financial and Capital Markets Commission (FCMC) was to make the same argument connecting the offshore sector to support for the fixed exchange rate in the face of adversity (see Chapter 6): "The Latvian financial sector operates as the regional financial centre partially, dealing with the non-resident customer money flow (…) This could be regarded as export of financial services that improves also the payment balance sheet in Latvia (FCMC 2012)

The corollary to the success of the IMF-inspired fixed exchange rate ideology was the *de facto* disenfranchisement of a significant part of the Russian-speaking population of Latvia, who comprised 42% of the total population of 2.7mn and nearly 50% of the population of the capital city Riga (Auers 2015). The disenfranchisement was the result of the newly independent Latvia's citizenship laws, which restricted citizenship to those who could trace their family to Latvia before its annexation by the Soviet Union during the Second World War. This move excluded from citizenship most of the Russian-speaking population, who had moved to Latvia following the war in the wake of the Soviet-driven industrialization (Auers 2015, Lieven 1994). This meant that the industrial collapse that resulted from the implementation of an IMF-backed monetarist policy, based on a strong Lat pegged to a basked of currencies, did not cause political reversals as it did elsewhere in the former Soviet countries, since it hit the disenfranchised Russophone population hardest. "In Latvia, the exclusion of the Russians from a political role meant that the mainly Russian managers and workers had far fewer means of influence to bear - least of all on Repše" (Lieven 1994 p364). In an interview, a former finance minister described how developing the offshore banking sector fitted into the emergent Latvian political economy:

> At the beginning of the 1990s you have an economy which is just emerging from the Soviet Union in this brave new world of market economy and they have economically three assets: one, transit - this was main gateway from the East to the West, in the new specialisation of labour where the east largely exports raw materials natural resources the ports have quite a bit of significance; two, agriculture; three, industry. They have dreams and memories of the so-called golden era, the times when Latvia was independent before the 1940s, when Latvian was largely agriculture. They face the challenge of a large Russian-speaking minority, which at that time was 40%, and more in the cities. Their challenge is to break down the resistance of the Russian-speaking minority, so they decide to do away with industry because the Russians largely work in

> industry. The new political elite decided to do away with industry, focus on agriculture, but agriculture is not something you can build a successful economy on. So they thought 'transit', and they thought 'we're going to be become a financial centre' based around the transit. This was quite an explicit policy in the early 1990s, to do away with industry and start building a financial industry. [interview #19, former Latvian finance minister]

Thus, in this way, the policy of attracting Russian flight capital was intended to support a strong and stable Lat as the foundation of economic independence under neoliberal macroeconomics. This is one of the answers to the paradox of why Latvia's new national political class, broadly hostile to Russia, supported the development of a banking sector based on Russian money, and often Russophone (Lieven 1994).

Repše and his deputy Ilmārs Rimšēvičs - who succeeded Repše as head of the Bank of Latvia from 2001-2019 after Repše entered politics - had a laissez-faire approach even to prudential bank regulation, as exemplified in the reluctant and belated intervention regarding Bank Baltija in 1995. Thus Latvia's non-resident banking system was built from the start on an absence of regulation, rather than any regulatory ring-fencing (interviews #5 US expert, #24 former Latvian manager). In particular this meant the absence of any requirement for customers of Latvian banks to use the domestic currency and / or to have any presence in Latvia. Sweeping deregulation, rather than regulatory ring-fencing, in this key area was the foundation of non-resident banking in Latvia as envisaged by Repše. This self-recusal from regulation is reminiscent of that of the Bank of England declining to regulate dollar transactions in the 1950s, as described above, which gave birth to the Eurodollar market, and led to the UK becoming, like Latvia on a much smaller scale, an OFC despite having neither regulatory ringfencing nor low tax regime (Palan 2003, Zoromé 2007). While, as noted above, there are parallels between the emergence of Latvian and Panamanian OFCs, Latvia never emulated Panama in creating offshore ringfencing legislation on corporate secrecy or low tax. Instead, the absence of banking restrictions in Latvia on currency of bank deposits and domicile of bank customers allowed Latvian bank customers to incorporate as shell firms registered in tax havens such as Panama, owning US dollar deposits, and thus enjoy the tax freedom and secrecy of the offshore space (interview #5, US academic). At the same time, because offshore banking in Latvia was not dependent on any legal provisions besides an absence of bank regulation, Latvia did not qualify as an OFC according to the methodology used by the OECD (interview #12 former auditor). Therefore, it was not subject to heightened scrutiny in the context of OECD and EU measures against unfair and harmful tax competition. Latvian developed a banking sector that was de facto offshore, but de jure on shore, which was to be its hallmark. I refer to the Latvian banking sector handling foreign currency deposits, mostly dollars, for non-residents, as ‘offshore banking’. In the next chapter I discuss other terms used by the banks and regulators.

The laissez-faire policy towards the banking sector as a whole and non-resident banking in particular went further. At a time in the 1990s when ‘money-laundering’ was still largely associated with narcotics trafficking, regulators such as Repše and Rimšēvičs were not inclined to restrict flows of money from Russia, a country to which the Latvian political elite were broadly hostile, since these flows supported the Lat, and by extension Latvian independence. “Money will work there where it is interesting for it to do so”, Bank of Latvia deputy head Rimšēvičs told Russian journalists in 1996. “There is no doubt that the money of new Russians, new Ukrainians and new Uzbeks and even Latvians themselves is very comfortable and interesting in Riga (…) Money will go there where it can earn and no amount of effort can make it stay elsewhere. Even if you patrol the airport with dogs, money will leave "(Ekspert 1997). Rimšēvičs told Russian journalists on another occasion that “capital flight from Russia - it is her and only her problem” (Segodnya 1996). As I shall discuss below, as the FATF regime gained global traction after 2000, this laissez-faire policy regarding the origins and legality of money entering the banking system was to develop after 2000 into an informal policy of ringfencing the offshore banking sector from the new anti-money laundering regulations.

Crucially, the bankers themselves believed that cold relations between Latvia and Russia were beneficial for the banking business, because in the eyes of Russian customers it strengthened the level of protection of their money in Latvia.

> The only business that has prospects against the background of the bad relationship between Russia and Latvia, is banking. … It created a guarantee that the Baltic states would keep their deposits secret from hostile political discovery … The government will protect the banking sector because it is a source of enrichment of the country (Kargins 2005 p229-232).

Thus, despite the different ideological currents of regulators pushing the Latvian nation-building project and the emerging partly Russophone banking sector, there was a confluence of views between regulators and banks on the desirability of a non-resident dollar sector catering to Russians and other former Soviet countries, and of a minimalist regulatory approach to the sector. Offshore banking in Latvia provides a rare case where the offshore financial centre is in a largely hostile relationship to a country that is a major source of funds; this dynamic can be explained by the financial practices of the offshore centre being in conflict with the interests and legislation of the source countries. This contrasts with the model usually found in the literature as described above of offshore centres being within the political orbit of the source of funds (Haberly and Wojcik 2013a).

5.4 Correspondent banking and black cash in Latvia's offshore banking sector in the 1990s

The integration of Latvia's banking sector into global finance took place in the 1990s via the international correspondent banking network, as it did across the CIS. Many of the dozens of small banks that characterised the banking sector in the 1990s met the description cited above of banks that "deposit all of their funds in, and complete virtually all transactions through, their correspondent accounts, making correspondent banking integral to their operations" (BINLEA 1999). By 1994, the Bank of Latvia noted that "[t]he liberal foreign exchange regime, the stability of the national currency, the favourable geographical position of Latvia as well as the wide network of correspondent accounts with foreign banks contributed greatly to the rapid development of Latvia's banks (Bank of Latvia 1994). Many banks had more international correspondent relationships than they did local branches in Latvia.

Transaction banking – that is, making international payments within the fastest possible time using the correspondent banking network - was one of the main services offered by any Latvian bank, and a bank's network of correspondent banks a key part of their marketing. Banks' entries in the Latvian business directory for 1994, for instance, mostly list the respective banks' entire correspondent network, together with basic data such as address, opening hours. "The wide network of correspondent bank relations continues to develop," reads the report of Baltic International Bank for 1994, one year after its founding. "It is the intention of the bank to become a powerful settlement centre, providing its clients the ability to make payments in any currency, in any country of the world. The bank has the power to precisely arrange settlements with the same day value which is a determining factor for many operations" (Baltic International Bank 1994). Parex Bank in 1994 detailed that "at the turn of 1991 and 1992 in Latvia there emerged an urgent necessity for need for a strong financially strong bank that could transfer and convert money both in the eastern and western countries … among Parex Bank's clients the biggest Latvian and CIS banks and corporations occupy the major position. They are attracted by the efficiency and speed at which the payments are made and by the possibility to open numbered accounts" (Parex Bank 1994). Riga Commercial Bank in 1994 claimed that thanks to its correspondent network and introduction of state-of-the-art banking technologies, clients could "make payments to any country within several hours" while Baltic Transit Bank cited transfer times of within 24 hours (Riga Commercial Bank 1994). A brief history of Latvian Credit Bank in 1994 placed the correspondent accounts on equal footing with branches, reading simply:

> January 20, 1992 - the foundation date of the bank. 1992 - branches opened in Aluksne, Bauska, Madona and Preili regions of Latvia. Correspondent accounts opened in Baku, Hamburg, Kiev, London, Moscow, Minsk, New York, Paris, Rotterdam, Stockholm, Tolyatti and Warsaw. 1993 - core capital of 5 million Lats [ca $10mn] registered (Latvian Credit Bank 1994)

Rietumu Bank's report for 1994 provided details of the value of transactions performed through the correspondent bank network. The name 'Rietumu' names means 'Western' in Latvian, and it was established by US citizens of Soviet origins in 1992. In 1994, the bank had only 24mn lats ($48mn**)** in assets - 5% of the value of transactions via its correspondent accounts. In 1994 Rietumu used its correspondent banking network to make a total of $614 million worth of payments for clients (Rietumu Banka 1994). "The network of international correspondent banks of Rietumu allows its customers to make payments effectively and quickly to any country in the world (…) we are permanently expanding the network of correspondent banks all around the world," the bank said in its report of 1994.

In Latvia, banks that focused on the correspondent banking business were regarded as more progressive and desirable than those focused on the unscrupulous pyramid-style high-interest resident deposit business or insider lending to related parties, especially after the collapse of Bank Baltija and the loss of many depositors' savings (Euromoney 1994). As described above, in the 1990s the establishment of extensive correspondent bank relations went hand in hand with the introduction of new banking communication technologies such as SWIFT and micro/cA$h. Banks' introduction of such technology was widely seen positively as part of Latvia's integration into global finance and financial innovation:

> Indeed, Latvian banks were pioneers in mastering the newest banking technologies which have enabled them to offer their customers very fast and convenient international transactions. This was contributed to by the very high percentage of IT and engineering specialists from the Soviet era who found employment in the banking system [interview #15 MP].

The Bank of New York scandal: implications for Latvia

According to the Association of Latvian Commercial Banks in 1999, 10 Latvian banks had correspondent accounts at Bank of New York. Other sources mention as many as 20 in total, the discrepancy perhaps due to banks having been closed before 1999 (Block and Weaver 2005). While there was little direct reference to Latvian banks in the US coverage of the BoNY scandal, which was focused on Russia due to the partisan political controversy, interview partners with knowledge from the 1990s confirmed there was significant involvement of Latvian banks:

> … all the dodgy money and the crooks and the shifters… Western banks jumped in very fast and facilitated all of this. And that was very frustrating. (…) Memories of Bank of New York (…) swamping off the money and mopping it off and providing all the facilities (…). And the IMF were very concerned that a lot of criminal money and money that was being looted out of Russia, selling state assets and just looting the money was going on here in Latvia. (…) And Riga was the main conduit, the money ended up partly in Swiss bank accounts and another such havens. (…) I had met Lucy Edwards [Bank of New York officer later convicted of money laundering in the US] in my office in Latvia. And I told her straight that she I felt she was facilitating money laundering through Parex Bank. And she didn't like my story. But it was clear from the volumes that were going through Parex at the time. [interview #23 former manager at Latvian bank]

There was also strong signs of involvement of Latvian banks in the BoNY scandal in media reports at the time, including money embezzled by Ukraine's prime minister Pavlo Lazarenko, later imprisoned in the US, and billions laundered out of a Ukrainian bank (Dienas Biznes 2002, Kommersant 2002, Biznes & Baltiya 2000).

Table 9. Latvian banks' US correspondent banks in 1999

Latvian bank	*US correspondent accounts*
Aizkraukles banka	Bank of New York
Baltijas International Bank	Bank of New York
Baltijas Tranzitu banka	Bank of New York; Citibank N.A.
Hansabanka	Bankers Trust Company
Latvijas Biznesa banka	Bank of New York; Riggs Bank N.A.
LATEKO banka	Bankers Trust Company
Latvijas Krajbanka	Bankers Trust Company
Latvijas Tirdzniecibas banka	ABN-AMRO Bank N.Y.; Republic National Bank of New York; First Union National Bank
MeritaNordbanken Latvia	Bankers Trust Company
Latvijas Hipoteku un zemes	Bank of New York
Multibanka	Bankers Trust Company; Credit Lyonnais New York Branch; Republic National Bank of New York
Ogres Komercbanka	Bank of New York
Parex Bank	Bankers Trust Company; Bank of New York
Banka Paritate	Bank of New York
Rietumu Banka	ABN-AMRO Bank New York; Bank of New York; Bankers Trust Company; Republic National Bank of New York
Saules banka	American Express Bank; Bankers Trust Company
Trasta komercbanka	Bankers Trust Company; Republic National Bank of New York
Latvijas Unibanka	Bankers Trust Company; Bank of New York; Republic National Bank of New York; Citibank; American Express
Ventspils Apvienota Baltijas	Republic National Bank of New York
VEF banka	Bank of New York
Vereinsbank Riga	Citibank N.A.; Harris Bank International Corporation

(Source: Association of Commercial Banks of Latvia 1999)

However, Latvian banks largely escaped the reputational fallout from the BoNY scandal, which hit Russia badly. Russia's 1998 default and the ensuing BoNY scandal - with two ensuing US Senate investigations into Russia-linked money laundering - was disastrous for Russia's reputation and led to US banks closing correspondent accounts for Russian banks *en masse* (US Senate 2001). Russia and Ukraine were subsequently blacklisted by FATF, as described below, which further interrupted their correspondent banking relations. Latvian banks' US correspondent banking relations, on the other hand, largely remained intact, leaving Latvian in a strong position to offer dollar transaction services to Russian and CIS banks. In 1999, a US manager from a correspondent bank told Latvian press that "[a] lot of time will pass now before Russian money will have direct access to foreign banks. For the meantime, Latvia has become the bridge between West and East" (Biznes & Baltiya 1999). Given the crucial importance of US correspondence accounts to the dollar-denominated offshore banks in Riga, a major task of these banks became to foster good relations with US correspondent banks, as I shall discuss in the next chapter (interview #24, former Latvian bank manager).

Practices of offshore banking in Latvia in the 1990s: Cash, shell firms and secrecy

Latvian banks' practices and products towards their customers in the 1990s bear many hallmarks of what from today's perspective would count as money laundering, since it involved accepting large cash deposits with no explanation of origin. In combination with the correspondent account network, these secret funds could then be moved through the international financial system to banking jurisdictions such as Switzerland or US. Since Latvia only passed an anti-money laundering in 1998 (see below) they were largely legal at the time (interview #23 former Latvian bank manager). Nevertheless, it was clear that these banking practices targeted the giant shadow economy of the CIS countries, in particular in handling large volumes of cash of unexplained origins, while providing high levels of secrecy. Thus, what now, in the context of the global AML regime, is called money laundering, could also be described more broadly with respect to the former Soviet countries as the integration of the CIS shadow economy into global correspondent banking.

In their public image, Latvian's non-resident banks often profiled themselves as 'private banks' on the model of Switzerland. Thereby private banking was often a euphemism for acceptance of large quantities of cash in anonymous deposits (interview #6 former Latvian banker). This explains the stress laid by banks on the physical proximity to Russia, since cash was safer to transport via a land border than as an air passenger. Physically transporting cash out of the country in the 1990s remained a key channel for moving money out of Russia, according to FATF reports at the time (FATF 1995, Kargins 2005). Parex in particular courted notoriety in Russia with a brash prime time TV based on the slogan "Closer than Switzerland" - openly encouraging wealthy Russians to deposit secret funds at Parex.

Following on the success of this ad, Parex launched another ad that referenced the Swiss flag as a plus sign: “we have many pluses - we are closer, faster and quieter than you think.” ‘Closer’ was again a reference to acceptance of cash deposits brought out of Russia, ‘Faster’ was a reference to the speed at which international payment transfers could be made, ‘quieter’ a reference to banking secrecy. Another famous Parex TV ad from the 1990s for the Russian market showed a Latvian country boy break open the family piggy bank and take the bag of coins into town to a bank, where he asks the cashier - “You won’t tell Mum?” To which the cashier answers gravely, “We guard our clients’ secrets” (Kargins p221). Other banks’ marketing materials likewise guaranteed customers secrecy. In 1994, Baltic International Bank described its business model thus: “The basic philosophy of BIB is Private Bank - Private Life: Private Bank guards private life, private bank defends private life, private bank develops private life (Baltic International Bank 1994). Latvian banks initially opened anonymous bearer deposit accounts for non-residents (Kargins 2005). After bearer accounts were banned in Latvia, banks continued to offer numbered accounts, where the identity of the account owner was known only to the top management of the bank (Moneyval 2007).

As discussed, many accounts were opened at Latvian banks as corporate accounts in the name of an offshore shell firm, which the swingeing banking deregulation discussed above allowed (interview #2 editor of Latvian bank journal, #5 US-Latvian academic, #15 Latvian MP) . In the post-Soviet context, shell firms allowed CIS individuals and companies to secretly control structures outside the country. When interacting with these structures in import or export deals, whether based on genuine or falsified paperwork, the shell firm anonymity and banking secrecy allowed the CIS structures to deny that the shell firm banking in Latvia was a related party. The incorporators of such shell firms also acted as business introducers or marketing departments for the banks, selling an offshore company in a package together with a bank account at a Latvian bank.

The role of offshore shell firms and business introducers will be dealt with in more detail below, but it is clear that already in the 1990s the banks organised a pipeline of offshore firms for prospective clients [Interview #15 Latvian MP, Figure 3]. A US expert based in Latvia in the 1990s recalls how even the state-owned savings bank Kraibanka had a side business setting up offshores for non-resident clients for tax evasion purposes, “a business which was considered so dirty that the bank created separate entities to handle it" [interview #5, US-Latvian academic].

Figure 3. Website of an offshore vendor from the 1990s

INTERNATIONAL OFFSHORE SERVICES can arrange for the opening of Offshore company accounts at many leading European banks. The exact choice of country and bank - in Western, Central or Eastern Europe - is the decision of the client.

For example, one of most widely used new possibilities for offshore banking is opening of corporate accounts in Latvian banks. The **Republic of LATVIA,** in The Baltic States, is a former member state of the USSR which achieved independence in 1991. Since that time, the country has enjoyed a period of economic liberalisation and rapid growth. In particular, Latvia has developed a profitable and effective banking sector which offers high-quality, confidential banking services, and is now a significant financial centre for clients from Eastern and Central Europe. Latvia is already regarded as 'the Switzerland of Northern Europe' and intends to continue the development of its growing financial sector. Latvian banks are now a popular choice for the establishment of a corporate account for an Offshore Company.

ADVANTAGES OF A CORPORATE BANK ACCOUNT IN LATVIA:

- **Easy procedures** for account opening, with minimum 'red tape' and reference requirements.
- **Strict confidentiality of** banking services.
- Operation of bank accounts in any currency, or operation of **Multi-Currency accounts** (i.e. transactions in US$, DEM, CHF, GBP, all on one account!)
- Sophisticated **electronic banking services**, including account operation via PC/Internet, allowing account access and information 24 hours each day, 365 days of the year!
- **Credit and Debit card services**, including corporate and personal Electron, Visa, Mastercard, and Diners Club card services.
- Instant availability of foreign currency **cash and Travellers Cheques**.
- **Excellent English** is spoken by the staff of Latvian banks, allowing for easy communication with international customers.

(Source: www.ioserve.com)

Latvian banks also developed channels for accepting undeclared cash deposits in Russia itself, according to extensive reporting in Russian media at the time and some Russian law enforcement actions (Biznes & Baltiya 1996b). Russian business media reported in the second half of the 1990s on activities of Latvian banks, for instance when Russian tax police alleged that offices at the Latvian embassy in Moscow were accepting cash for deposit in Latvian banks (Ekspert 1997). Other Latvian banks had no official office in Russia, but ran secret offices that accepted cash (Ekspert 1997). Latvian banks worked with secret cash in a different way, according to further reports. This involved schemes to 'convert' off-the-books cash of funds held in banks, in Russian known as '*obnalichivanie'* or '*obnal'* (Izvestija 1999). This operation is a major pillar of the shadow economy in the former Soviet states. It aims to enable clients of the scheme to evade VAT by their making payments to the operators on fictitious contracts, thus generating a fraudulent tax credit for the clients. The operators then return the funds to the clients as off-the-books cash, which can be used to pay salaries evading payroll tax (Yakovlev 1999). This operation involved transfer of money out of the country under fictitious contracts to an offshore account in a Latvian bank. But instead of being paid further to accounts in the West, the money would be returned to the originator as 'black cash' via a number of different permutations and intermediaries (Segodnya 1996, Biznes & Baltiya 1997).

5.5 Conclusion

This chapter has described how offshore banking emerged in Latvia in the aftermath of the collapse of the Soviet Union, and the financial operations in which it specialised. One reason for this was the powerful independence movement in Latvia that moved towards monetary independence and currency liberalisation before the rest of the Soviet Union, with Latvia a pioneer in forex cash trading already in 1991. This in turn created a powerful bank lobby after Latvia achieved full independence that shaped bank regulations in its favour. Secondly, the leadership of the Bank of Latvia was strongly monetarist and laissez-faire in ideology. It saw development of the banking sector using funds from the CIS states as a way to support the newly introduced Lat and compensate for the decline of Soviet industry after introduction of market economy principles. The role played by Latvia in Russian commodity exports in the 1990s created a basis for this. Offshore banking thus emerged as the result of the Latvian financial regulator's laissez-faire deregulation of currency and banking sector, not through tailored offshore regulation. Thus, Latvia, in some ways like UK, did not qualify as an OFC according to regulatory characteristics, but thanks to deregulation acted as an "offshore banking hub" - using the concept developed by Binder - while in legal terms being onshore (Binder 2019).

While initially the financing of Russian export operations drove the rapid expansion (and criminalisation) of the new banking sector, banks quickly established a niche in meshing global correspondent banking with the embryonic commercial banking sector across the former Soviet space, which dealt largely in shadow economy monies. This led to transaction patterns emerging that were later revealed in investigations of the BoNY scandal in the US, comprising networks of shell firms operating via US correspondent banking accounts to make payments between the CIS shadow economy and global financial system using fake documents and frequent redundant payments, which from today's perspective would be termed 'money laundering'. In the 1990s, as US correspondent banks indiscriminately engaged with banks across the CIS space, Latvia accounted for only part of this business. Its particular niche at the time was accepting undeclared cash on deposit for transfer through correspondent accounts, hence the advantage of Latvia's geographic proximity to the CIS.

By the 1990s much of the business of offshore banking in Riga was to mediate between CIS shadow economy cash and global electronic funds transfer systems. Because Riga banks targeted the post-Soviet shadow economy, the increasingly hostile relationship between Russia and Latvia was supportive of Latvia's offshore banks, providing clients assurance that their money would be safe. Riga became an offshore financial centre for the CIS that unusually had a hostile relationship towards its main source of funds. Latvia's divergent foreign policy trajectory from the CIS states also meant that it was largely shielded from the reputational fallout from the BoNY scandal of the late 1990s. In the next chapter I will show how after 2000 Riga became one of the main sites for integrating the CIS shadow economy into US dollar correspondent banking despite Latvia's implementation of FATF rules and accession to NATO and EU.

Chapter 6. Whitelisting Latvia: Reputation and reality of offshore finance and AML in Latvia

6.1 Introduction: Latvia and lists

This chapter examines Latvia's shifting geopolitical alignment 1995-2018, and how Latvia's pro-Western path 'whitelisted' rather than eliminated the post-Soviet offshore financial sector examined in the previous chapter. The theoretical framework for this chapter is derived from the governmentality approaches to the global AML / CFT regime discussed in Chapter 3, in particular the discussion of blacklisting, greylisting and whitelisting. While however scholars have focused largely on blacklisting and greylisting, I focus on their flipside, i.e. de facto whitelisting, denoting in a broad sense the successful avoidance of blacklists and greylists as constituting de facto whitelisting:[1] In a regime where blacklisting and greylisting play a major role, those entities successfully avoiding blacklists and greylists can be considered to be de facto whitelisted, i.e. to be "entities judged to be safe or trustworthy" (Bedford 2016 p35).

'Whitelisting' thus refers here to a number of processes - some targeted, some coincidental - that elevated the status and reputation of Latvia's offshore financial sector out of the 1990s post-Soviet context into what Latvian regulators called "Western civilization", despite the operations of the offshore sector established in the 1990s growing rapidly post-2000 (FCMC 2015 p6). I will show in this chapter that these 'whitelisting' processes enhanced rather than reduced the Latvian financial sector's role in integrating the CIS shadow economy into US correspondent banking. Such whitelisting processes include Latvia joining the European Union and NATO in 2004; the integration of Latvia's domestic banking into European banking via the expansion of Scandinavian banks on the domestic market; the targeted lobbying of US regulators; and even the early adoption of sophisticated but ineffective anti-money laundering laws. 'Whitelisting' in this sense does not refer to any actual whitelist, but is a metaphor for Latvia's accrual of low-risk attributes.

[1] There is of course no actual whitelist within the FATF regime, but I use the term as shorthand to denote the successful avoidance of being blacklisted or greylisted.

Whitelisting of Latvia can be operationalised by the FATF blacklists and greylists (see Table 10).[2] Latvia has never been on the blacklist or greylist, despite expectations in Latvia in 2019 that Moneyval would greylist it in 2020 (interviews #9 former adviser to Latvian prime minister, #10 former Latvian financial market official, AML official #14 former Latvian finance minister). While Latvia is classified by IMF research as an OFC on the statistical strength of the high ratio of financial services provided to nonresidents, as discussed, it is not a low tax or secrecy jurisdiction and thus does not feature on any of the OECD, EU, US and other lists of tax havens engaged in harmful tax competition (Zorome 2007).

Table 10. Countries currently or previously on the FATF greylists (since 2010) and blacklists (since 2000)

Greylisted	*Greylisted and blacklisted*	*Blacklisted*
Afghanistan	Algeria	Cayman Islands
Albania	Bahamas	Cook Islands
Angola	Bolivia	Dominica
Antigua and Barbuda	Cambodia	Egypt
Argentina	Cuba	Grenada
Bangladesh	Ecuador	Guatemala
Bosnia and Herzegovina	Ethiopia	Hungary
Botswana	Ghana	Iran
Brunei Darussalam	Indonesia	Israel
Guyana	Kuwait	Kenya
Honduras	Myanmar	Lebanon
Iceland	Namibia	Liechtenstein
Iraq	Nicaragua	Marshall Islands
Kyrgyzstan	Nigeria	Nauru
Lao PDR	Pakistan	Niue
Mongolia	Panama	North Korea
Morocco	Philippines	Russian Federation
Nepal	Sri Lanka	Saint Kitts and Nevis
Papua New Guinea	Syria	Saint Vincent and the Grenadines
Paraguay	Tanzania	Sao Tome and Principe
Serbia	Thailand	Turkey
Sudan	Turkmenistan	Uzbekistan
Tajikistan	Ukraine	
Trinidad and Tobago	Vietnam	
Tunisia	Yemen	
Uganda	Zimbabwe	
Vanuatu		
Venezuala		
Serbia		

(source: FATF)

[2] While FATF also uses the terms 'blacklist' and 'greylist', the blacklist is formally known as the list of "High-Risk Jurisdictions subject to a Call for Action" and the greylist the list of "Jurisdictions Under Increased Monitoring." (FATF 2021)

Latvia has also received positive assessments from the most authoritative benchmark index of countries' AML standards, the Basel Anti-Money Laundering Index (available since 2012). The EU draws on the Basel AML Index to compile its list of high-risk countries. The Basel AML Index is strongly informed by the published results of the FATF Mutual Evaluation Reports, the specifics of which I will discuss further below.

Table 11. Latvia's ranking according to the Basel Anti-Money Laundering Index

2012	5.36 (48 from top)	2016	4.91 (37 from top)
2013	4.93 (34 from top)	2017	4.44 (13 from top)
2014	5.03 (42 from top)	2018	3.98 (12 from top)
2015	4.98 (41 from top)	2019	4.89 (44 from top)

(Source: Basel Anti-Money Laundering Index)

The Basel AML Index groups countries with ranking from 0-3.3 as low risk, 3.3.-6.6 as medium risk, over 6.6 as high risk, meaning that Latvia received a 'medium risk' assessment. However, it should be noted that in 2012-2017, for each year only two countries received 'low risk' assessments, five all told: Norway, Finland, Estonia, Lithuania and Slovenia.

Table 12. Top 40 Basel AML Index (2013) Bottom 40 Basel AML Index (2013)

1 Norway	21 Ireland
2 Slovenia	22 Colombia
3 Estonia	23 Romania
4 Finland	24 Jamaica
5 Sweden	25 Poland
6 Lithuania	26 Czechia
7 Malta	27 Oman
8 New Zealand	28 Slovakia
9 Hungary	29 Saudi Arabia
10 Bulgaria	30 Georgia
11 Chile	31 Great Britain
12 France	32 Armenia
13 Belgium	33 Singapore
14 South Africa	34 Latvia
15 Iceland	35 Netherlands
16 Portugal	36 Moldova
17 Montenegro	37 Israel
18 Denmark	38 Egypt
19 Peru	39 China
20 Australia	40 Canada

129 Namibia	149 Afghanistan
128 Lebanon	148 Iran
127 Angola	147 Cambodia
129 Algeria	146 Tajikistan
128 Trinidad Tobago	145 Iraq
129 Liberia	144 Guinea-Bissau
128 Lesotho	143 Haiti
127 Sierra Leone	142 Mali
126 Nigeria	141 Swaziland
125 Niger	140 Mozambique
124 Zimbabwe	139 Laos
123 Togo	138 Kenya
122 Benin	137 Uganda
121 Tanzania	136 Nepal
120 Dominican Rep.	135 Paraguay
129 Cape Verde	134 Zambia
128 Papua New Guinea	133 Burkina Faso
127 Vietnam	132 Yemen
126 Mauritania	131 Argentina
125 Venezuela	130 Bolivia

The Basel AML Index is highly influential, and informs major commercial providers of Country Risk Rankings. Nevertheless, each bank and other regulated bodies draw up their own inhouse country risk assessments that incorporate Basel AML Index together with other indices and their own assessments. These may be more inclined to reflect overall indicators of good governance, for instance such as EU membership (Interview #29, UK AML officer). Thus the country risk assessment of an international bank shared by an interview partner put Latvia in the low risk group, while placing USA in the medium risk group, likely for tax compliance reasons (Table 13).

Table 13. Country risk ranking used by a European bank

Low risk (56)	Medium Risk (65)	High risk (70)
Barbados, Belgium, Bermuda, Botswana, Brunei, Cape Verde, Cayman Islands, Chile, Croatia, Cyprus, Czech Republic, Denmark, Dominica, Estonia, Fiji, Finland, Georgia, Germany, Gibraltar, Greece, Guernsey, Hong Kong, Hungary, Iceland, Ireland, Isle of Man, Japan, Jersey, South Korea, Latvia, Lesotho, Lithuania, Luxembourg, Macedonia, Malaysia, Malta, Mauritius, Namibia, Netherlands, New Zealand, Norway, Oman, Poland, Portugal, Qatar, Romania, Singapore, Slovakia, Slovenia, Spain, Sri Lanka, Swaziland, Sweden, Switzerland, United Kingdom, Uruguay,	Albania, Algeria, Argentina, Australia, Austria, Bahamas, Bahrain, Belize, Benin, Bhutan, Brazil, British Virgin Islands, Bulgaria, Burkina Faso, Canada, China, Colombia, Cook Islands, Costa Rica, Dijbouti, El Salvador, Ethiopia, France, Gabon, Ghana, Germany, Italy, Jamaica, Jordan, Kazakhstan, Kuwait, Kyrgyzstan, Liechtenstein, Madagascar, Malawi, Mali, Mauritania, Mexico, Monaco, Mongolia, Mozambique, Nepal, Niger, Panama, Peru, Puerto Rico, Rwanda, Samoa, Saudi Arabia, Seychelles, South Africa, St Lucia, St Kitts and Nevis, St Vincent and the Grenadine, Taiwan, Tajikistan, Tanzania, Timor-Leste, Togo, Trinidad and Tobago, Turkey, UAE, United States, Vietnam, Zambia	Afghanistan, Angola, Armenia, Azerbaijan, Bangladesh, Belarus, Bolivia, Bosnia and Herzegovina, Burundi, Cambodia, Cameroon, Comoros, DRC, Congo Republic, Cote d'Ivoire, Cuba, Northern Cyprus, Dominican Republic, Ecuador, Egypt, Equatorial Guinea, Eritrea, Gambia, Guatemala, Guinea, Guinea-Bissau, Guyana, Haiti, Honduras, India, Indonesia, Iran, Iraq, Israel, Kenya, North Korea, Kosovo, Lao DPR, Lebanon, Liberia, Libya, Moldova, Montenegro, Morocco, Myanmar, Nicaragua, Nigeria, Pakistan, Papua New Guinea, Paraguay, Russia, Senegal, Serbia, Sierra Leone, Somalia, Sudan, South Sudan, Surinam, Syria, Thailand, Tunisia, Turkmenistan, Turks and Caicos Islands, Uganda, Ukraine, Uzbekistan, Vanuatu, Venezuela, Yemen, Zimbabwe

Source: provided by interview partner

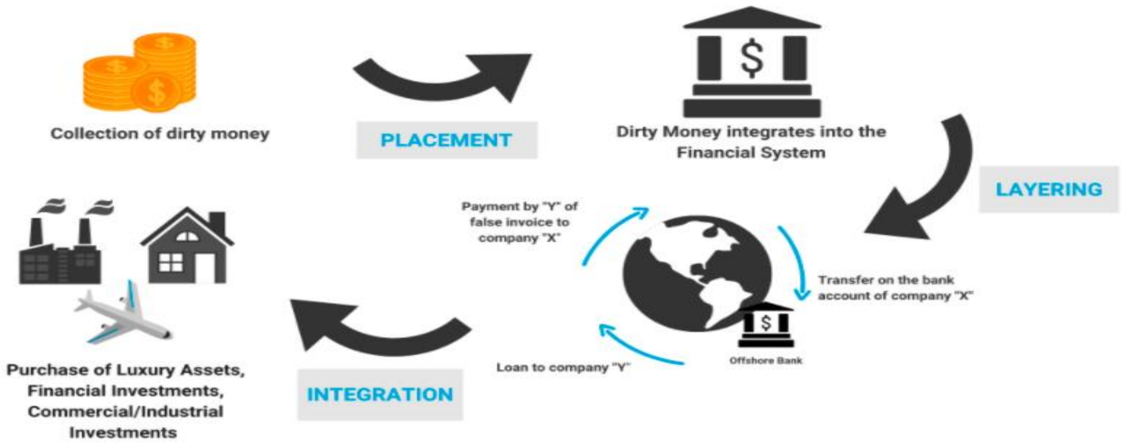
It should be noted that Latvia was listed as a “country of primary concern” for money laundering by the United States Bureau of International Narcotics and Law Enforcement Affairs. However it shared this status with all of the G7 nations including the USA itself, making the status not relevant for transaction screening (BINLEA 2011).

6.2 Performing money laundering

To examine the impact of AML on the geography of offshore finance, we need to examine the relationship between AML and money laundering itself and explain how money laundering and anti-money laundering interact with each other in practice. Two possible outcomes to the question of how AML impacts on offshore banking in Latvia would seem to be that either AML cleans up the offshore finance sector in Riga, or that AML ‘kills’ it off because the Riga financial centre is so dependent on ML that without it, it loses coherence and purpose. As we will see in the narrative, the main development in Latvia was a quite different one - rapid growth of the offshore sector without change in practice - which requires a more sophisticated understanding of the interaction between money laundering and anti-money laundering.

What is money laundering? While there is an extensive literature on anti-money laundering, there is a much smaller literature on money laundering itself. The AML literature often repeats the definition of anti-money laundering of institutions such as FATF, which sees money laundering as a three-step process - placement, layering and integration, as shown in Figure 4 (Unger 2017, Unger 2013).

Figure 4. The Money Laundering Cycle Source: (UNODC website)



A recent critical overview of money laundering however attempts to define what exactly constitutes the difference between money laundering as opposed to the simple management of criminal assets:

> Smuggling money, burying it in the garden or buying high value assets is still mere handling or managing of assets which remain tainted if not covered by a specific action, namely the *false* justification of their origin. This false justification is strictly laundering in the meaning of pretending a licit origin of the acquired assets ('white washing'). (Van Dune et al 2018 p94, original italics)

Thus, the authors define money laundering as: *"a justifying activity intended to falsely legitimise or 'whiten' (an) unlawfully obtained asset(s) or advantages(s)"* (Van Dune et al 2018 p94, original italics). To a post-structuralist ear, the term "a justifying activity" as definition of money laundering has clear hallmarks of performativity, since it is ultimately a claim - "pretending a licit origin" - that can succeed or fail:

> [T]he concept of performativity has lead to the replacement of the concept of truth (or non-truth) by that of success or failure (…) We are no longer in the register of truth as a reference but - to stick to the same word - in that of truth as success or failure, in truth as fulfilled conditions of felicity." (Callon 2007 p320-321)

Treating money laundering as performative raises the question of what conditions does money laundering reference when attempting to make money appear clean? What are the 'conditions of felicity' for illicit money to be judged licit? I argue that under the conditions of the global anti-money laundering regime outlined in the previous chapter, the 'conditions of felicity' that money laundering need to fulfil are determined by the AML regime itself and its network. This network ranges from government regulators such as financial intelligence units and law enforcement to screening software, banks' AML departments and the private compliance and due diligence sectors. Money laundering has to reference whitelists of perceived low risk categories for success.

As discussed in Chapter 3, scholars working in the governmentality paradigm define whitelists as "classification systems and technologies that pre-authorise action or access for entities judged to be safe or trustworthy" which "involve place-based judgements about trustworthiness" that "purport to classify trust, worthiness, and reputation" (Bedford 2016 p31, p35). While there is no FATF or other AML whitelist per se, the proliferation of blacklists, greylists and AML rankings means that there is a de facto whitelist of countries, comprising those that have not featured on blacklists or greylists and rank well across various AML indices. Thus we can talk of whitelisting by default to denote countries ranked as low risk and absent from blacklists and greylists.

This opens a fresh perspective on how money laundering and anti-money laundering interact. Money laundering refers to AML risk assessment lists because these define the "conditions of felicity" for the money launderers' "justifying activity" Van Dune et al 2018 p94). Money laundering needs to pass AML tests to be successful. Thus, the interaction between offshore finance, money laundering and the AML complex becomes more intricate if we view money laundering as a performance that references the global AML regime. This means that I regard here the AML complex itself as part of the assemblage of money laundering.

While this 'whitelisting' argument seems counterintuitive, on a human level, it is well accepted that winning trust by claimed or apparent reputation and status goes hand in hand with fraud: "the sociology of fraud is inseparable from the sociology of confidence" (Harrington 2012 p393). As one of the respondents noted anecdotally, "I have never met a money launderer who wasn't a nice guy (…) Lucy Edwards and Peter Berlin [Bank of New York official and husband prosecuted for Russian money laundering] were two of the nicest people you could ever hope to meet" [interview #8, former AML officer in US bank]. It is also known that organised crime carefully studies AML technologies to comply with them (Beckert and Dewey 2017).

Performance, whitelisting and geography

The practice of whitelisting and blacklisting is highly geographical. One of the key indicators used to assess money laundering risk is 'country risk', the risk assigned to the respective country where an individual or legal entity involved in a transaction is based. The reason for 'country risk' serving as such an important marker in anti-money laundering risk assessment, despite its obvious lack of granularity, originates with the politics of blacklisting and sanctions, as the enforcement mechanisms adopted by the US and allies with the aim of installing the AML regime globally. Since the rollout of the global AML regime is based on the threat of sanctions against non-compliant individual states, money laundering risks are primarily assessed for states as units of analysis (Sharman 2009). The level of (non)compliance with FATF of a respective country is thus equated to actual money laundering processes in that country, justifying the sanctioning of countries on the basis of their failure to implement FATF recommendations.

This means that the country level has become a key marker of money-laundering risks above that of individuals or individual entities. As discussed, beyond the FATF black list, the private sector maintains its own more extensive blacklists and grey lists, entered as parameters in anti-money laundering screening software, and determining on the basis of risk assessment whether enhanced due diligence, i.e. in-depth analysis, should be applied to a transaction or not. Country-level risk plays a major role in such assessment. In cases where a country receives a high-risk assessment, the bank may simply decide to block all transactions with that country, or raise charges to cover the cost of 'enhanced due diligence,' which can directly impact on the country's economy (interview #29).

Secondly, since there is little accountability or room for appeal in such categorization of countries according to money laundering risks, countries can be obsessive about their reputation to preempt any downgrading, as noted in Chapter 2. Whitelisting in a broader sense is thus a question of reputation. OFCs place "almost mystical faith" in the value of a reputation, while reputational damage caused by blacklisting lasts after a country is removed from the FATF blacklist, analogous to having spent time in jail (Sharman 2011p). "Host governments promote their OFC's respectability, and with careful (and costly) public relations manufacture an image of probity" (Hampton and Christensen 1999 p7). An IMF report on OFCs found that "it is most likely that the major competitive factor in the current international environment is an OFC's established reputation" (Suss et al 2002 p18). A number of researchers into offshore financial centres personally reported being themselves upbraided by local representatives concerned about a potential besmirching of the reputation (Hudson 1996, Sharman 2011). During this research project, while Latvia was threatened with relegation to the Moneyval / FATF greylist, a number of potential interview partners referred to this process when declining interviews, in case they jeapordised Latvia's 'whitelisting'.

Because of the structural financial and military power of the US and EU within the AML regime - with each maintaining their own blacklists - a third aspect of white and blacklisting is networking with these as allies. As I will argue below, there is an expectation in 'frontline' NATO allies such as Latvia of special treatment from the USA. Conversely, we see that following the exit of United Kingdom from the EU, the EU for the first time blacklisted UK overseas territory Cayman Islands as a tax haven, in the absence of British political protection (Guardian 2020c). A Russian official argued that FATF's blacklisting of Russia in 2000 could have been prevented, had Russia's diplomats been quicker to demand representation in FATF in the 1990s. "That's what it means to belong to these 'clubs'" (Ekspert 2000).

I refer to the overall positive assessment of a respective jurisdiction in the context of AML as whitelisting. By whitelisting I mean firstly the specific practice of FATF/Moneyval evaluations and their reflection in benchmark indices such as the Basel Anti-Money laundering Index as reviewed above. Secondly, I mean positive market reputation. Despite the difficulties of measuring this, major markers, for example membership of perceived 'good governance' areas such as EU and Eurozone, can cement a country's positive reputation, especially for small countries. Thirdly, I mean whitelisting in an extended sense referring to the networking with the sites of power that determine white, grey and blacklists, ultimately with the Western financial-security establishment (De Goede 2012, Palan 2010). Thus whitelisting is an ongoing process of negotiation.

The remainder of the chapter is divided into four sections. In section 5.2., I look at how major post-Soviet countries Russia and Ukraine, having suffered reputational damage as a result of the 1998 default and BoNY scandal, were then blacklisted by FATF in 2000-2003. In contrast, in section 5.3 I examine Latvia's successful pro-Western trajectory, and its implications for the offshore banking sector during the boom years 1998-2008, and during the financial crisis in 2008 through to Latvia's joining the Eurozone in 2014. In section 5.4, I look at Latvia's early adoption of AML institutions such as Financial Intelligence Units and superficial success in implementing the FATF recommendations, as evaluated by Moneyval's mutual evaluation process. In section 5.5, I show how financial flows through Latvia surged after 2000 while retaining the same structure of transaction banking as in the 1990s.

6.3 Whitelisting Latvia

Following the debacle of the 1998 rouble crisis and the 1999 BoNY scandal, in 2000 FATF placed Russia on its first blacklist of 'non-compliant countries and territories', designed to "name, shame and punish" those listed. (FATF 2000, Gilmore 2011 p61). This was a formal confirmation of the shattered status of Russia (and Ukraine) following the 1998-99 financial debacle after years of optimistic rhetoric of market reform. Given Russia's reputation was already damaged, the direct implications for Russian banks' continued access to US correspondent accounts was more significant than the wide reputational effects, since the measure required banks to "give special attention to business relations and transactions" with all Russian entities (FATF 2000). As detailed in Chapter 5, the BoNY scandal had already led to a largescale withdrawal of many US banks from the Russian market. Russia was removed from the blacklist in 2002 after enacting anti-money laundering legislation (FATF 2002). However, the US later placed sanctions on international banks such as ABN-AMRO that it alleged were facilitating money laundering out of Russia (Wall Street Journal 2004). The full FATF sanctions were applied to Ukraine from 2002 to 2004. FinCEN issued a notice under Article 311 of the 2001 USA PATRIOT Act designating Ukraine as a "country of primary money laundering concern" (FinCEN 2003). Ukrainian press reported the closure of correspondent accounts following the ruling, and quoted Ukrainian bankers lamenting that "even if Ukraine will be removed from the blacklist at the next FATF meeting, we still be left laundering our reputation, and this is a lot harder" (Kommersant 2003).

In contrast to the blacklisting of Russia and Ukraine, Latvia's international credentials went from strength to strength in the wake of the 1998-99 crisis. This divergence in status between Latvia and the CIS strengthened Latvia's position as a channel between the post-Soviet financial system and the US dollar banking system, as US banks became reluctant to deal directly with the myriad of small banks operating across the former Soviet space.

The groundwork for Latvia's whitelisting was laid in 1995, when Latvia's potential future membership of NATO and EU was established (European Union 1995). In June 1995 Latvia, Lithuania and Estonia signed an association agreement - also known as a 'Europe Agreement' - with the EU, which symbolised the "the return of the Baltic States to the European family" (European Union 1995). In 1995 the NATO member states also decided to enlarge the alliance eastwards to incorporate the most 'successful' of the former socialist countries, based on the results of its published 'Study on NATO Enlargement' (NATO 1995). In 1999 NATO recognised Latvia as a membership aspirant and launched a Membership Action Plan for NATO, paving the way for accession in 2004. In December 1999, the summit of the EU heads of states and governments took the decision on EU enlargement allowing Latvia to open accession negotiations with the EU (Auers 2015, Latvia MFA). The end of the process came in 2004, as Latvia joined both the EU and NATO, the first and to date only post-Soviet countries to do so, in a move that redrew the political and security map of Europe. In 2006, a NATO summit was held in Riga, for the first time on the territory of the former Soviet Union, focusing on NATO's heightening military campaign against the Taliban insurgency in Afghanistan. Latvia had supplied troops to the US military campaigns in both Afghanistan and Iraq (NATO 2006). In May 2005, Latvia adopted the European Exchange Rate mechanism, the prelude to adopting the Euro as currency on January 1, 2014. Finally, in 2016, Latvia was accepted into the OECD, completing Latvia's integration into almost all the top 'clubs' of nations (MFA Latvia, Aslund 2017, Auers 2015).

This revolution in Latvia's geopolitical status had implications for Latvia's access to the US dollar banking system. Being part of 'the West' was to become an ultimate point of appeal for Latvian banks to have access to dollar correspondent accounts (FCMC 2015). As I shall show at the end of this chapter, the progressive integration with the 'West' was accompanied by a surge in financial flows through Riga, with no change in the nature of the money from the 1990s. A former adviser to Latvia's PM noted:

> There were big hikes [in financial flows] like for instance when Latvia joined the EU, that I think gave new impetus to the offshore sector, then after we joined the Eurozone that gave another sort of boost, because a lot of this money is looking for the EU and Western seal of approval. [interview #9, former adviser to Latvian prime minister]

Expansion of Scandinavian banks and emergence of a hybrid banking sector

Starting in the late 1990s, Swedbank and SEB, two of Sweden's four largest banks, moved onto the Baltic market through acquisitions (Koernert 2017). The Swedish banks in Latvia acted as the main channel for the global credit boom, triggering a rapid economic expansion. On the back of the credit boom, Latvia together with Lithuania and Estonia achieved high growth rates averaging 10% 2004-2007, earning them the sobriquet 'Baltic Tigers' (Koernert / Romanova 2014). By 2015, Swedbank held a market share in Latvia of 17.3%, SEB 11.3% and Norway's DNB 7% measured by assets (Koernert 2017). The effect of the arrival of the Scandinavian banks was to change the overall reputation of the Latvian banking sector from being post-Soviet to being semi-Scandinavian. Because reputation and country risk assessment is on the level of the individual jurisdiction, the dominance on the retail market of the Scandinavian banks served to effectively whitelist the Latvian banking sector as a whole, including the offshore banks. For example, scholarly accounts of Latvian banking have omitted the offshore element entirely by focusing on the role of the Scandinavian banks (Koernert 2019).

As a result of the entry of the Scandinavian banks into the Latvian market, a hybrid banking sector developed comprising two distinct banking models. The Latvian regulator Financial and Capital Market Commission (FCMC) defined the first group of banks as those whose "business is oriented towards the [Latvian] domestic market," i.e. the Scandinavian banks, who dominated Latvia's retail market. The second banking segment was the dollar offshore market, in the hands of mostly home-grown banks, some with CIS-based shareholders. The FCMC designated these banks as "banks that do business with non-residents and service cash flows of non-residents," abbreviating this to "banks for non-resident depositors" (FCMC 2012 p84). As mentioned above, the offshore banks referred to themselves mostly as "private banks." I mostly use the more straightforward term 'offshore banks' and 'offshore banking' to refer to this banking segment.

Table 14. Two groups of banks in Latvia

Banks oriented towards serving the domestic market	*Banks doing business with non-residents*
Subsidiaries and branches of European banks	Locally-owned or CIS owners
Credits make up around 72% of assets	30% of assets, securities 20% and the rest of funds are held on correspondent accounts to ensure fast settlement of payments for customers
Funded by parent banks and resident deposits	Funded over 75% by on-demand non-resident deposits.
Earning from interest	Earning from commissions and currency exchange fees

Source: adapted from FCMC 2012 annual report (FCMC 2012)

Table 15. Latvian market shares of Scandinavian and non-residents banks 2014

	Assets	*Total deposits*	*Non-resident deposits*	*Total lending*
Scandinavian	60%	45%	20%	77.4%
Banks for non-resident depositors	40%	55%	80%	22.6%

(Source: FCMC 2014)

Table 16. Ownership of Latvian banks in 2014

Name	Assets	Ownership
Swedbank	€4.93bn	*Swedish parent*
SEB	€3.97bn	*Swedish parent*
ABLV	€3.07bn	Latvian owned, Luxembourg affiliate
DNB Nord	€2.36bn	*Norwegian parent*
Rietumu Bank	€2.35bn	Latvian owned
Citadele	€1.91bn	Former Parex bank, nationalized in 2008, privatised to US investors in 2014
Latvijas Businesa Banka	€0.86bn	Russian owned
Privatbank Latvia	€0.77bn	Ukraine owned, Cyprus, Italian and Swiss affiliates
Latvijas Hipotēku zemes banka	€0.51bn	*State-owned savings bank*
Trasta Komercbanka	€0.49bn	Ukraine/Latvia owned, Cyprus branch
Baltikums Bank	€0.47bn	Latvian owned
Regionala Investiciju Banka	€0.43bn	Ukraine owned, Luxembourg branch
SMP Bank	€0.33bn	Russian owned
Latvijas Pasta Banka	€0.32bn	Latvian owned
Rigensis Bank	€0.27bn	Latvian owned

Source: (FCMC 2014) (Domestic-market-oriented banks in italics)

There was also some convergence between the two groups, as the global credit boom that fuelled the Scandinavian expansion also prompted some offshore banks to raise funding on international markets before 2008 in order to launch mortgage loans on the local market. Parex Bank, the leader in this connection, shifted from calling itself a ‘private bank’ to a ‘universal bank’ (Parex 2007). Using investment grade credit ratings from Moodys and Fitch, in 2005, Parex issued Latvia’s first non-sovereign Eurobond for $100mn, raising almost $1bn in bonds and short-term syndicated loans between 2000 and 2008. Conversely, following the collapse of the Scandinavian banks’ retail market strategy during the financial crisis 2008-2010, their Baltic subsidiaries entered the booming offshore dollar market, ultimately suffering reputational damage for doing so in the form of money laundering scandals that broke belatedly after 2015 (Clifford Chance 2020).

Offshore sector support for NATO and the West

Networking with major powers is a successful strategy on the part of offshore financial centres to avoid blacklisting, scholars have established. OFCs blacklisted by FATF were "disproportionately stigmatized because they lacked powerful allies" while Latvia was arguably one of those lucky OFCs excluded from FATF lists thanks to "politicking" (Palan et al 2010). Alone on military strategic grounds, Latvia could count on US backing for exclusion from FATF listings similar to that provided to Panama, also a strategic US ally (Van Fossen 2003). In similar fashion France protected Monaco, UK Bermuda, British Virgin Islands, Gibraltar, Isle of Man and Jersey, while Canada protected Antigua and Barbuda as well as Belize from FATF listings (Van Fossen 2003). Latvian offshore banks were thus involved in constant networking with US representatives, regulators and correspondent banks over their continued relationship after the turn of the century, because of the centrality of US accounts to their high-risk activities. This networking drew on the broader Latvia-US relationship as "strategic partners," as celebrated by both countries (Auers 2008). Crises such as the US PATRIOT Act Article 311 notice against two Latvian banks in 2005 discussed in Chapter 8 only intensified the lobbying and networking efforts, as we shall see.

A former manager at a leading Latvian offshore bank in the first years of the new century recalled:

> It seemed to me that the biggest fear of [the bank] was getting blacklisted, having its correspondent account shut down for money laundering. So there was constant relationship building with the corresponding banks and even having (…) more corresponding banks than we needed so that if some of the accounts would shut down they would still be able to operate. But I understand the challenge for us as we kept getting caught again and again and again in corruption scams. And each time we got caught in another corruption scandal it put our correspondent accounts in jeopardy [interview #4, former manager at Latvian bank]

A competitor bank was equally involved in lobbying in US, using personal connections to get a meeting with a top official in the US Federal Reserve. In the meeting, the official sought clarification on what activities could count as money laundering in the eyes of US regulators.

> I can tell you that we were all being viewed as a bunch of money launderers so I tried to explain what we were trying to do. And then they came around to understanding that this was a bank. We were operating in a fire zone trying to do it right. I asked this guy, who was a very senior guy in the Fed at the time, I said, can I name money laundering activities for you, and you tell me yes or no, and we went through all those we mentioned, trafficking, extortion, guns arms bla bla bla, and his head was nodding, and I then I said, taxation. He paused and he looked at me. He said, ah, taxation. He said, it's the national sport in every country, the evasion or the avoidance of. And I was basically saying, how do I know the Russian client has complied with Russian taxation. It may be a forged document. He might not be able to get a document. God knows what I am dealing with. So it's a very difficult area. So one never really knew [interview #23, former Latvian bank manager]

To counteract such misapprehension on the part of the US, the offshore banks leveraged Latvia's relationship with NATO to lobby for continued access to US dollar clearing. The offshore banks, and Parex in particular, were strong supporters of NATO accession before 2004. Afterwards they hired former US diplomats closely involved with the NATO expansion policy as lobbyists in Washington to secure continued access to correspondent accounts. Parex was a sponsor of events flanking the 2002 Prague and 2006 Riga summit (Kargins 2005, Wall Street Journal 2007). "They were very well aware of the fact that the business model was dependent on the good graces of the people in Washington. And they, you know, in various times tried to, you know, try to make sure that they were on the right side of that" (interview #21, Latvian journalist).

The support for NATO was part of a broader lobbying campaign Parex and other offshore banks conducted via professional lobbyists in Washington DC. The aim of the lobbying was to upgrade the reputational status of the banks, leveraging Latvia's membership of NATO as an argument to secure access to US correspondent accounts (Wall Street Journal 2007). In parallel to such solo efforts, in 2005 five other offshore banks established the 'Latvian-American Financial Forum' (LAFF) with the intention "to enhance development of the Latvian financial centre, its competitiveness worldwide, and the transparency and responsibility of the business environment (…) to facilitate economic cooperation between Latvia and the USA, (…) as well as ensuring new advantages for Latvian capital in the USA (ABLV 2005 p27). LAFF was later rebranded as the Latvian Private Bank Association, tasked with ensuring “a favourable environment for promoting financial service exports, as well as strengthening the professional reputation of private banks.” The Association of Latvian Commercial Banks, which included almost all the offshore banks, was also active internationally in directing “a voluntary private sector initiative aimed at strengthening the relationship with correspondent banks, particularly in the United States.” (Moneyval 2009).

Table 17. Top Western officials on boards of, or shareholders in, Latvian and Latvia-linked offshore banks

Western official	source
former CIA head of counterterrorism (Josef Cofer Black)	(BIB website)
former head of German foreign intelligence (August Hanning)	(Norvik 2017)
former secretary general of NATO (Andres Fogh Rasmussen	(PNB 2018)
former German representative to NATO (Hans Friedrich von Ploetz)	(BIB website)
former Republican US presidential candidate (Bob Dole)	(Global Witness 2010) (Latvia-linked Kyrgyz bank)
family friend of incumbent US vice president (Devon Archer)	(Norvik 2015)
former head of US Federal Reserve (Paul Volker)	(Wall Street Journal 2014, Citadele 2016)
former president of World Bank (James Wolfensohn)	(Wall Street Journal 2014, Citadele 2016)

Lobbying in the corridors of power in US continued after 2008, when individual banks attracted top former Western officials from the security, political and financial establishment as directors or as minority shareholders in order to raise their reputational status (Table 17). The focus on former Western security-linked officials again referenced the strategic significance of Latvia as being on NATO’s ‘frontline’ with Russia, in particular after the Ukraine crisis of 2014. Latvian offshore bankers also maintained informal ‘hobnobbing’ networks with Western elites. One respondent recalled how a photo of a Latvian banker with UK’s Prince Charles hung in the banker’s office, and how Donald Trump Junior had been keynote speaker at the main Baltic offshore banking conference in 2012 (interview #16, Latvian investigative journalist). A banker likewise recalled his photo opportunity at the

White House with then Vice President Joe Biden (interviews #6, former shareholder in Latvian bank).

Ultimately, Latvian regulators argued that Latvia's overall whitelisting as "a part of Western civilization" entitled it to US correspondent accounts:

> I think that we as the Eurozone and NATO state, as a part of Western civilisation, should be given a possibility to ensure with our AML/CTF regime that there are financial institutions in Latvia for the direct settlement of accounts in US dollars (FCMC 2015a p6).

Protecting the offshore sector during the financial crisis of 2008-2009

Scholars of offshore financial centres have analysed the closely-knit and personalised politics that characterise such jurisdictions (Hudson 1996, Roberts 1995, Hampton and Christensen 1999, Palan et al 2010). These have two vectors: firstly, the political interdependence between government and the offshore sector along the lines "we need them, and they need us" (Hudson 1996 p121); secondly, personal and business relationships cutting across institutional boundaries (Hampton and Christensen 2003). Latvia had similar networks between the finance sector and politics. This was true not just of the politicians of the 1990s, as described in the previous chapter, but also for the 'New Era' party created in 2001 on an anti-corruption agenda and led by the former head of the Bank of Latvia in the 1990s, Einars Repše, and his protégé Valdis Dombrovskis, who together formed a government 2002-2004 and again in 2009. Offshore bankers were among the party's supporters and also Repše's personal business partners (interviews #19 former Latvian finance minister, Baltic Course 2008). At the same time, Latvia's governments enjoyed a favourable international reputation in securing the transition to democracy and market economy and joining NATO and the EU. They were thus both inclined to and able to defend the offshore sector internationally. In the context of whitelisting, the fact that Latvia's government was on the side of the offshore banks played an important role during the financial crisis of 2008-2010 in protecting the offshore sector.

Given the high exposure of Latvia's banking sector to external wholesale funding from Scandinavian parent banks or international capital markets, and the widely diagnosed overheating of the Latvian (and Baltic) economies, the credit crunch starting 2007 impacted quickly on Latvia. The global financial crisis sparked by the Lehman Brothers bank collapse in the US in early October 2008 then proved devastating for the country. The impact on the banking sector was immediate. On November 8, 2008, the Latvian government declared it would acquire 51% of Parex Bank for a token amount from the shareholders, and later acquired all of it. Parex confronted the impossible task of rolling over its syndicated loans, while facing a run on deposits (Aslund and Dombrovskis 2011).

As a result, Latvia had to inject 4.9% of GDP to recapitalise Parex with 2.6% of GDP in additional guarantees (Aslund and Dombrovskis 2011). Notably there was no debate about a bail-in of the Parex offshore depositors, as the EU and IMF would later implement in similar circumstances for Cyprus banks in 2013. While the strength of the offshore bank lobby in Latvia doubtless played a role in protecting the sector, bailins were simply not a recognised tool for handling a financial crisis on the part of international financial institutions at the time in 2008-9. Only in 2010 did international discussion start on the need for such a strategy (Economist 2010). As a result, the Parex shareholders walked away from their bank while the population paid the price of bailout and ensuing austerity.

Indeed, the Latvian state itself became a major shareholder in the non-resident business through its nationalisation of Parex, including Parex' Swiss subsidiary. At the time of nationalisation, Parex held 26% of non-resident deposits, and its largest individual client was said to be Gulnara Karimova, the daughter of the then president of Uzbekistan, who has since been both imprisoned in her homeland and indicted in the US for corruption (interview #1, Latvian investigative journalist, Guardian 2019). Subsequently the decision was taken to split Parex into a 'bad bank' and 'good bank', a strategy that had proved successful in Sweden in the early 1990s. The state-owned 'good bank' successor to Parex, rebranded as Citadele, continued to operate a substantial offshore business for the CIS states, including the Swiss subsidiary. It was re-privatised in 2014 to US investors (Citadele 2016). The bad bank 'Reverta' took on the non-performing assets, including a large portfolio of loans believed to have gone to the former shareholders (interview #24, former Latvian bank manager). The bailout of Parex again underlined the Parex shareholders' strong political influence in bearing no financial or legal consequences for the collapse of the bank (interview #24, former Latvian bank manager).

Despite the collapse of Parex, overall the offshore banking sector came through the crisis with its position strengthened, compared to the retail-focused Scandinavian banks (interview #23 former Latvian bank manager). This was because Latvia opted to repeat its policies of the early 1990s of maintaining a strong fixed Lat exchange rate through intense domestic austerity, as Latvia prepared to join the Eurozone (Aslund and Dombrovskis 2011). The policy was indeed implemented largely by the same ‘team’ as in the 1990s, with Einars Repše returning as finance minister to serve under his former subordinate Dombrovskis as prime minister in 2009, while Rimšēvičs remained in charge at the Bank of Latvia. In agreement with the IMF, Latvia embarked on a policy of ‘internal devaluation,’ radically slashing public expenditure and raising VAT to avoid a fiscal deficit of a size unacceptable to the European Central Bank. The effect of the financial crisis and austerity measures was an 18% collapse of GDP in 2009, overall from peak to trough 25% of GDP 2008-2010 in the world’s single biggest national recession during the global financial crisis (Aslund and Dombrovskis 2011). The swingeing austerity following on the global crisis caused mass impoverishment and emigration but eliminated Latvia’s balance of payments deficit (Hazans 2013).

As we have seen in the previous chapter for the 1990s, such a policy of maintaining the fixed exchange rate in the teeth of bitter recession pushed Latvia to nurture all incoming capital flows. ‘Russian’ money flowing through the banking system was a major resource in this context. Latvian regulators justified the “financial logistics” of the offshore banking sector as improving Latvia’s balance of payments (FCMC 2012a). Given the scale of the crisis, “Russian money and transactions were welcome,” while “authorities unfortunately cut resources available for investigations,” Latvian parliamentarians later told MEPs (European Parliament 2018 p14). As we shall see, dollar payments surged again after the 2008-9 crisis to reach tens of billions of dollars per day, peaking at an estimated 1% of global dollar transactions (Bloomberg 2018). The Dombrovskis government pursued policies explicitly aimed at bolstering the offshore sector, introducing a ‘golden visa’ programme aimed at wealthy CIS citizens. This programme rewarded foreign investors in real estate in Latvia with a five-year EU-wide right of residency (Rebaltica 2013). An alternative investment option to the Golden Visa was investment in the subordinated debt of Latvian banks (Rietumu 2010). This investment programme signalled Latvian government’s continued goodwill towards the offshore sector and wealthy CIS clients.

Latvia joined the Euro in 2014 after the imposition of this severe austerity programme that avoided monetary destabilisation and fiscal deficits. On the back of this perceived success, despite the heavy toll paid by the population, Latvian PM Dombrovskis became the European Commission’s Vice President for the Euro in 2014, subsequently also assuming responsibility for EU financial markets and AML, while his ally Rimšēvičs as head of the Bank of Latvia ex officio joined the governing council of the European Central Bank. The head of the offshore banks' US lobby, LAFF, writing in international press, celebrated Latvia's accession to the Euro as another whitelisting of Latvia's offshore sector.

> And here is a last reason why Latvia is eager to join the euro zone: We understand the higher standard applied to institutions in Russia's orbit. That's why our banks' anti-money-laundering standards are among the most rigorous, praised by everybody from the International Monetary Fund to the U.S. Treasury to MoneyVal, the Council of Europe's anti-corruption unit. We welcome the bright light shined by the euro. (Ronis 2013)

The following sections examine to what extent Latvia's AML standards were 'among the most rigorous, praised by everybody."

6.4 (Ap)praising Latvia's AML regime

Researchers on offshore financial centres have identified a pattern where OFCs adopt AML rules swiftly but once implemented these "are either not enforced or unenforceable" (Palan et al 2010 p206). One reason for such weak enforcement identified by researchers is that the "same people who are responsible for regulation and supervision of the offshore financial industries are also engaged in active promotion and solicitation," i.e. regulators also act as advocates (Roberts 1995 p252). Scholars have detected a similar pattern in Latvia of implementation of AML legislation without ensuing enforcement, "where corruption and weak penalties combine to undermine the formal compliance regime" (Bowen and Galeotti 2013). In this section, I discuss the institutionalisation of anti-money laundering in Latvia, without subsequent enforcement, in the context of the whitelisting process.

In November 1996, the three Baltic heads of government jointly signed the 'Riga Declaration' on combating money laundering, together with top representatives of FATF, the European Commission and United Nations International Drug Control Programme**.** In 1998, Latvia then passed a 'Law on the Prevention of Laundering the Proceeds from Criminal Activity' that fulfilled these commitments**.** Latvia's FIU started operations on June 1 1998, and joined the international Egmont Group of FIUs in May 26, 1999. It was the 47th member worldwide of a group that now totals 164. Thus Latvia can be regarded as an early adopter of the FATF regime. In its second-round evaluation of 2003, the Council of Europe's anti-money laundering committee Moneyval assessed Latvia's FIU as:

> a dedicated, professional and thorough FIU. They continue to be at the centre of the national anti-money laundering effort. They are adequately resourced and well supported by government. (Moneyval 2004 p3)

The second key AML institution in which Latvia was an early and successful participant by the end of the 1990s was the FATF-conceived system of rolling mutual evaluations, which in Europe was implemented by Moneyval. The first and second round evaluation reports (2000 and 2004 respectively) did not contain any rating of compliancy with FATF. However, the evaluations clearly gave Latvia an overall positive assessment, especially when compared with peer countries from among Eastern European states who were also candidates for EU membership. The 2000 evaluation reported that:

> Latvia has taken a number of significant steps to counter money laundering. They have put together a very comprehensive structure for the protection of the financial system in a regime based on suspicious and unusual transaction reporting, the latter with a range of different reporting thresholds for various institutions (Moneyval 2000 p5).

While the evaluations of AML in Latvia were not uncritical - critique points are discussed below - they were significantly more positive than for some other EU new members. Poland's 2000 evaluation for instance found that "[u]rgent action is required if Poland is to develop an effective operational anti-money laundering system that meets international standards" (FATF 2000).

Table 18. Compliant ratings in EU / EFTA countries in Mutual Evaluation (2005-2011)

Belgium	7	UK	13	Netherlands	21	Iceland	27
Slovenia	9	Bulgaria	15	Lithuania	21	Poland	28
Hungary	10	Spain	15	Ireland	21	Liechtenstein	28
Cyprus	10	Switzerland	17	Czech	22	Finland	28
France	11	Italy	18	Sweden	22	Monaco	29
Portugal	12	Norway	18	Romania	23	Slovakia	35
Malta	12	Latvia	20	Austria	24	Greece	36
Estonia	13	Germany	20	Denmark	25	Luxembourg	39

(Source: Moneyval)

In order to implement the anti-terrorism financing measures of the FATF Nine Special Recommendations on Terrorist Financing, Latvia passed a new AML law of 2008, which replaced the 1998 AML law. A third round of evaluations was concluded in 2009 (see Table 18). For the first time, Moneyval published the full evaluation reports, allowing to quantify and compare individual countries' levels of compliance with each other (Levi et al 2018). Latvia had only 20 partly or non-compliant ratings out of 49, putting it in the top half of EU countries on a par with Germany (Moneyval 2009). In the follow-up round, Moneyval assessed Latvia as partly compliant or non-compliant in only 14 recommendations of the 49 (Moneyval 2012).

The Basel Anti-money Laundering Index cited in the introduction draws heavily on the FATF mutual evaluation results. Latvia's good showing in the ranking was cited by pro-offshore bank accounts of Latvia's financial sector as proof that the money-laundering risks had been mitigated. This illustrates the whitelisting effect resulting from the comprehensive introduction of AML institutions (Aslund 2017). Latvia's advanced AML legislation was thus often (mis-)taken as a sign of low money laundering risks. Germany's FIU in 2005, alerted by US PATRIOT Act Article 311 notice against Latvian banks (see Chapter 8), concluded from Latvia's advanced AML legislation that Latvia did not present any heightened money laundering risk. "In fact, some of the laws enacted in Latvia go beyond the standards currently applied in Germany" (FIU Germany 2005 p34).

From enforcing regulation to defending reputation

Despite the apparent success in introducing AML institutions, Latvia's record in enforcement of AML laws was poor (Bowen and Galeotti 2013). Moneyval experts noted that while Latvia quickly implemented the legislative and regulatory requirements to achieve broad compliance with FATF recommendations, this was slow to produce any money laundering criminal investigations let alone successful prosecutions (Moneyval 2004).

This pattern of AML implementation without enforcement follows that of offshore financial centres such as Jersey, Cayman Islands and Switzerland (Hampton and Christensen 2002, Palan et al 2010). These jurisdictions displayed 'defensive reporting' strategies, meaning that they filed many suspicious activity reports based on a box-ticking approach which overwhelmed the financial intelligence units without leading to any prosecutions. “The rush to implementation might be a window dressing exercise rather than a genuine attempt to cooperate with the international community” (Hampton and Christensen 2002 p202). Therefore, reputational concerns can motivate a pattern of AML implementation without AML enforcement. Taken together, such a pattern comprises “strategies to avoid blacklisting” (Ferwerda et al 2019).

Similarly, in Latvia, much of the suspicious transaction reporting by banks to the FIU had the signs of ‘defensive reporting,’ according to the Moneyval evaluators. Banks reported any client transaction that met one or more of a list of criteria specified by regulators as red flags, rather than operating on the basis of a real founded suspicion on the part of the AML officer. Such ‘defensive reporting’ by banks led to the “submission to the Control Service [FIU] of significant numbers of reports with little or no value for FIU analytical purposes which in turn overwhelmed the resources of the FIU ” (IMF 2007 p95). A comparison between EU countries of suspicious transaction reports per capita per year in 2015 showed that Latvian banks filed 11.59 suspicion reports per capita, double the figure filed by UK banks per capita, with Germany at only 0.36 and Switzerland at 0.29 per capita (Ferwerda et al 2019 p5).

For Caribbean OFCs, it has been observed that regulators can be primarily concerned with reputation, which conflicts with their regulatory role (Roberts 1995). Similarly in Latvia, AML institutions quickly took on a role as international defenders of the reputation of Latvia’s offshore sector. The clearest example of this was the Council for Prevention of Laundering of Proceeds Derived from Criminal Activity. The Council was created in January 2005 as part of a government push to implement AML (FCMC 2010). The Council encompassed all top-level officials involved in regulating the finance sector: the chairman was the Prime Minister, and members included the relevant cabinet ministers, prosecutor general, and the heads of the Supreme Court, Bank of Latvia, and FCMC (Government of Latvia 2009). However, in April 2007, the body was renamed the “Finance Sector Development Council” (FSDC) and its priorities shifted from AML to promoting the offshore sector. Its overriding aim was now to “promote the international competitiveness of the financial sector and the export of financial services” and “to promote the recognition of Latvia as an international financial center abroad,” i.e. to act as a pro-bank organisation (Government of Latvia 2009).

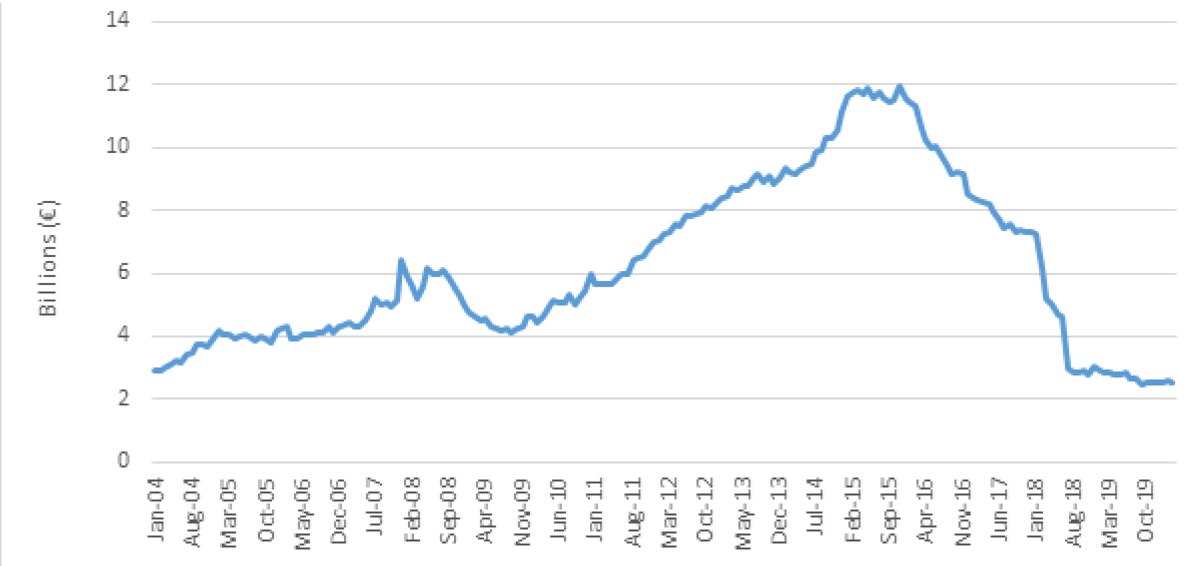
A similar oscillation between regulation and concern for reputation manifested itself at the the Financial and Capital Market Commission and Financial Intelligence Unit. In 2001, bank supervision including AML was devolved from the Bank of Latvia to a new autonomous body, the Financial and Capital Markets Commission (FCMC). In terms of anti-money laundering, FCMC responsibilities covered preventive aspects (FCMC 2010). Offshore banks argued that supervision by the FCMC was "among the strictest in all Central and Eastern Europe" (Parex 2005 p33). A later account sponsored by offshore banks lauded the FCMC as "a highly effective, qualified, and sufficiently large regulator … a top-notch financial regulator" (Aslund 2017). However, in reality, FCMC had powers to fine banks only up to 100,000 lats ($161,000) for AML breaches, but fines rarely reached even this insignificant level before 2016 (AML systems 2010, Moneyval 2004, Bowen and Galeotti 2013). FCMC remained informally under the influence of the Bank of Latvia and important positions were held by former AML officers of offshore banks (interviews #12,#19, FCMC 2015b, FCMC 2019b).

Both FIU and FCMC acted as international advocates of the offshore sector, vouching that the offshore sector had a legitimate business model and was properly regulated, referring back to the advanced AML legislation. This underscores that both organisations believed themselves to have a reputational mission beyond their regulatory remit: to defend the offshore sector against international criticism. Thus, in 2005, in response to two Latvian banks being designated as "institutions of primary money laundering concern" by FinCen (see Chapter 8), the head of the FIU filed a letter with FinCen, defending the reputation of the offshore banking sector (FinCEN 2005). In 2011, when questioned by journalists, the same official said that "the media have exaggerated the situation by republishing articles from the foreign press about yet another bank in Latvia which has been used as a transit facility for illegally obtained monies," adding that "dirty money represents only a small share of the total amount of money which passes through our banks" (Rebaltica 2012). The head of the FCMC likewise defended offshore banks against money-laundering allegations on several occasions. In an interview in 2012, he referred to Latvia's AML legislation to rebuff allegations of money laundering, calling the label 'money laundering' "insulting" and "mostly a myth". "Latvia is a member of the EU, which fulfils all AML requirements. The system is in place, we nurture and develop it under the watch of international experts" (Delfi 2012). In Chapter 8 I examine in detail the veracity of such claims, which I adduce here to point to regulators' conflicting concern with reputation.

6.5 Whitelisting and financial flows

During the years that saw Latvia increasingly integrated into 'Western civilization' according to FCMC - or as I term it 'whitelisted' - the amount of non-resident deposits increased by 600% peaking in 2015-2016, before US regulators intervened to put an end to the business in 2018 (FCMC 2015 p6). Thus, the successful institutionalisation of AML institutions was accompanied by a major expansion of offshore financial flows through Latvia.

Figure 5. Non-resident deposits 2004-2019 in billions of euros

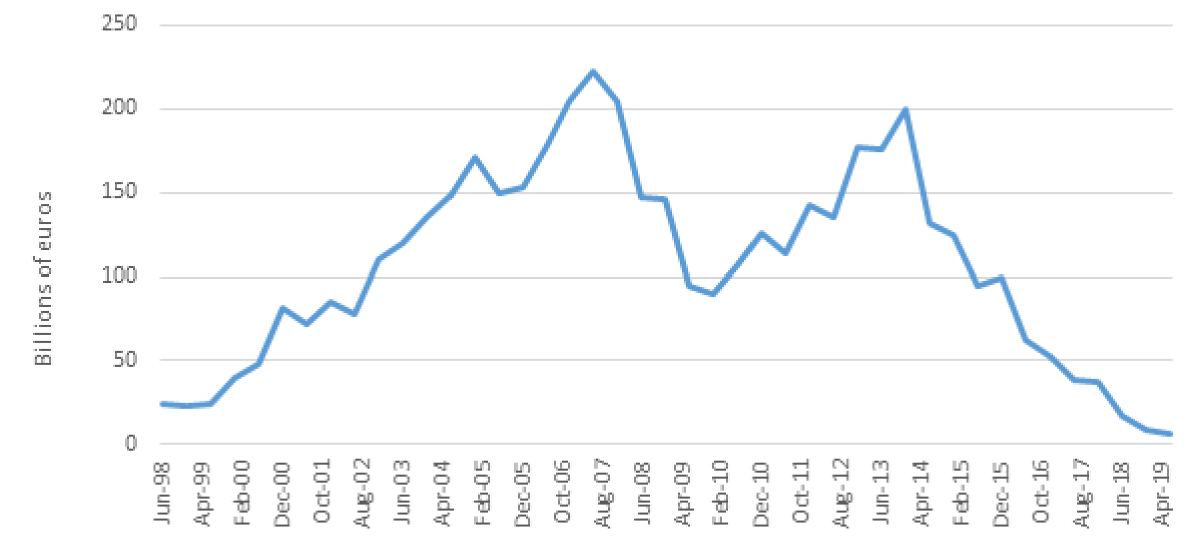


Source: Bank of Latvia

This shows that the whitelisting of Latvia and the implementation of AML institutions had not ended, but enhanced the post-Soviet offshore banking model established in the 1990s. This was not the sole reason behind the size of the surge in funds, which was also driven by commodity-driven economic growth in the post-Soviet countries, a strengthening dollar relative to the euro, and the Cyprus crisis in 2013.

Closer examination of the banking model shows that despite the official term for the banking model as 'banks for non-resident deposits,' the international transaction business examined in Chapter 5 was dominant. A large part of non-resident deposits were placed with correspondent banks, whereby the daily balances on the correspondent accounts were booked as overnight loans to the correspondent banks, as seen in the graphic below. Around one quarter of assets owned by offshore banks were held on correspondent accounts with European and US banks (FCMC 2012).

Figure 6. Total customer credit transfers not in Lats or Euros (in billions of Euros, 6 month totals)



Source: Bank of Latvia

While the payment volumes in the graph above are significant, reaching over $500bn per year, it is likely that the actual amount of payments made via Latvian banks was larger than captured within Latvia's national payment system. International media have cited US Treasury claims total Latvian transactions after 2010 had reached 1% of dollar transactions in the Swift payment system (Bloomberg 2018, Jemberga and Purina 2016). FinCEN estimates total daily dollar transactions in SWIFT as $5 trillion, thus 1% would be $50 billion daily. This is clearly a far larger figure than reflected in the official payment statistics depicted above. The figure '1% of SWIFT transactions' has become widely accepted for the size of transactions in Latvian discourse. A number of respondents confirmed the "1%" figure without however putting any more exact figure [e.g. interviews #15 Latvian MP, #14 former Latvian finance minister, interview #30 former US law enforcement officer]. The results of a survey of correspondent accounts of Latvian banks conducted by the Bank of Latvia in 2010 and 2012 do however suggest a figure of this order of magnitude. These 2010 and 2012 figures were collated by the Bank of Latvia in the framework of an European Central Bank survey of EU banks' correspondent accounts. The Bank of Latvia used the opportunity to gather information on Latvian banks' payments via the 1142 nostro accounts they had placed with foreign banks in currencies other than Lats or

Euros. These figures give daily totals of $16bn worth of transactions for March 2010 and $18bn per day for November 2012 (Bank of Latvia 2012 p24, Bank of Latvia 2010 p17). According to the Bank of Latvia, "[p]ayments on Latvian credit institution nostro accounts are effected outside Latvia's payment system," accounting for the discrepancy between the ECB survey figures and the figures for the payment system above (Bank of Latvia 2012 p24).

Respondents confirmed that Latvian offshore banking was more like a payments system than non-resident banking elsewhere in Europe.

> It was more transaction type of business. They were just using the payment system rather than like in Switzerland creating the higher value, (…) they were just using the infrastructure to channel funds back and forth, more like transit of money (interview #9 former advisor to Latvian PM)

> The kind of one key rule was that it was all short term. (…) There was the capacity to move it instantly. We would never lock it down into our banks (interview #18 former Latvian financial market regulator)

> As a rule they [deposits] were what I called one night stands. That was not something that was really seen in the Latvian economy and boosting its growth rate. Those are the short term deposits that were just coming in and out over and over over night. (interview #14 former Latvian finance minister)

Belatedly, following the US intervention in 2018, Moneyval identified precisely this high flow of payments via deposits as the sign of money laundering risk in Riga, rather than the size of the non-resident deposits per se. "Due to the transitory nature (…) the best measure of ML/FT risk exposure (…) is actual volumes of non-resident customers' payment *turnover* rather than by their deposit *amounts*, because low account balances on high payment turnover accounts may represent the same risk level, as those of higher balances" (Moneyval 2018, para 313, my italics).

Figures 7 and 8 show that non-resident customers of Latvia continued to incorporate predominantly as shell firms in secrecy jurisdictions. In the next chapter I will explore this topic of shell firms in more detail in the next chapter, in particular the use of UK as a jurisdiction to incorporate shell companies.

Figure 7. Non-resident corporate deposits in Latvian banks in 2011 by domicile of owner Source: FCMC[3]

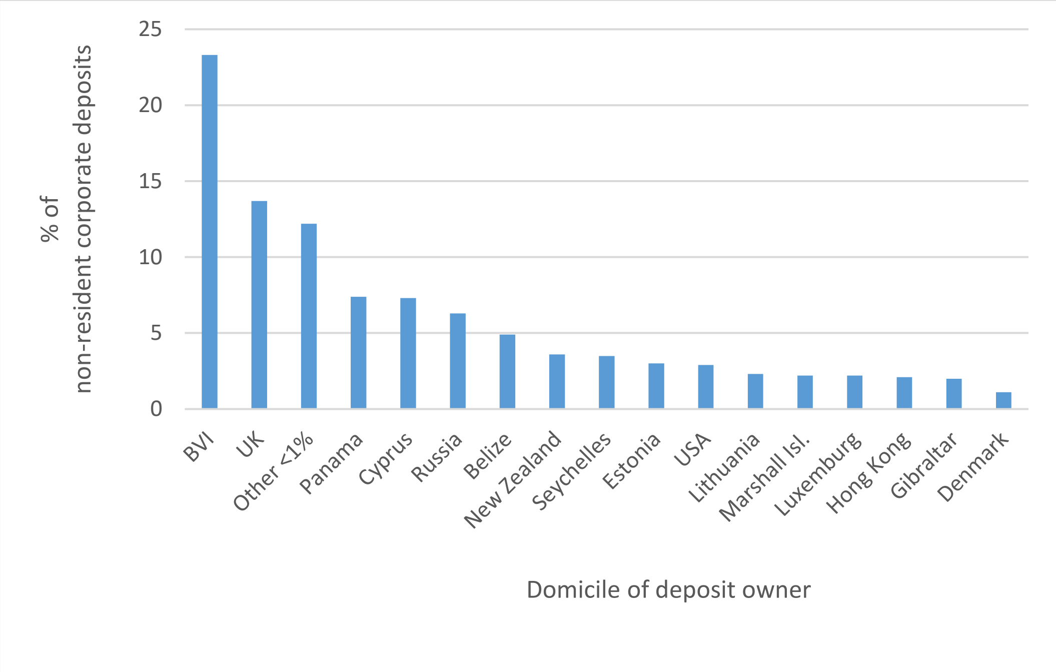
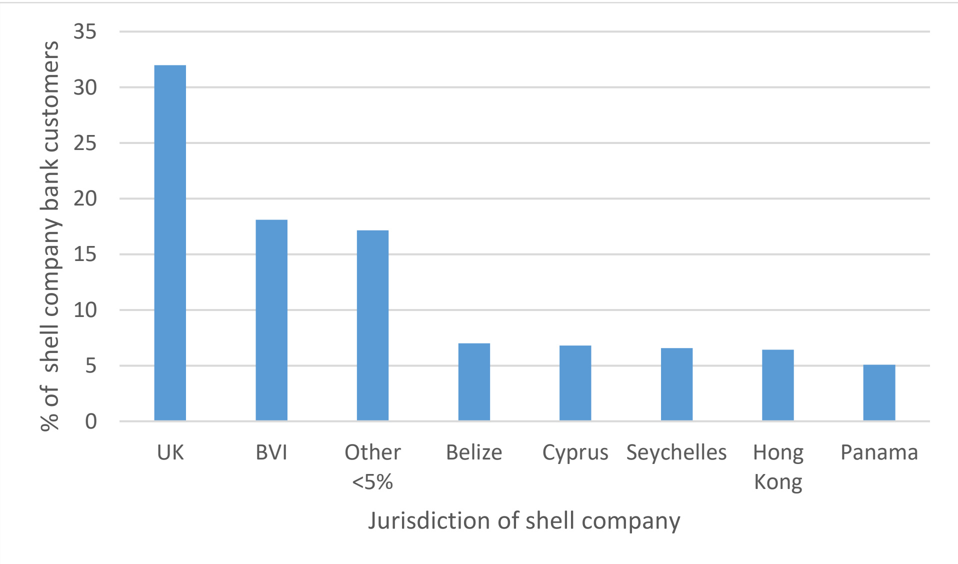


Figure 8. Domicile of shell company customers of Latvian banks in 2018



Source: FCMC 2018[4]

[3] Provided in email correspondence
[4] Provided in email correspondence 16.11.2018

Therefore, the institutionalisation of AML in Latvia was accompanied by a surge in the volume of offshore financial flows handled in Riga without any change in the structure of transactions from the shadow-economy business of the 1990s. I shall examine the nature of these financial flows in more detail in the next chapter.

6.6 Conclusion

Using the theoretical discussion in Chapter 4 of governmentality and the technology of lists,this chapter has discussed how Latvia's path with respect to the FATF regime diverged from the CIS countries post-1998. While Russia and Ukraine found themselves blacklisted by FATF in 2000-2003, Latvia found itself fast tracked to join the elite club of member of NATO and EU, the ultimate 'whitelist'. All of this firmly placed Latvia in the camp of what Latvia's financial regulators called "Western civilisation" (FCMC 2015 p6). Regarding the banking sector, Latvia's European integration in the credit boom years led to rapid expansion of Scandinavian banks on the domestic market, overshadowing the offshore sector. Latvia's NATO membership similarly helped legitimise Latvian banks access to US correspondent banks, despite disruptions such as the 2005 Patriot Act Article 311 notices against two banks, which I examine in Chapter 8. At the same time, Latvia was an early and successful adopter of anti-money laundering institutions as set down in the FATF 40 Recommendations.

But while Latvia was whitelisted by the governmentality technologies of the AML / CFT regime, the offshore banking sector inherited from the 1990s boomed, without changing its business model. Thus Latvia can be described as an 'onshore OFC'. According to formal criteria, as well as networks and reputation, Latvia was an onshore jurisdiction, with advanced AML framework, a banking sector dominated by Scandinavian banks, a respected EU member and a strategic relationship with the US. At the same time Latvia played host to a booming offshore sector, which as I show in the next chapter, was predominantly involved in shadow economy activities for the CIS countries. As I have argued, Latvia's onshoreness and whitelisting facilitated the development of the offshore sector and its work in mobilising the CIS shadow economy for financial capitalism. In the next chapter, I will examine the offshore business by tracing its shell firm clients, exploring one of its major markets, and examining an individual bank, using digital data sets combined with interviewing.

Chapter 7. Latvia as a shadow-economy OFC: 'Prestigious' shell firms, laundromats, and the financial institutionalisation of corruption

7.1 Introduction

This chapter examines the work performed by the Latvian offshore sector in integrating the CIS shadow economy into US correspondent banking, i.e. Latvia's role as an OFC for the shadow economy of the CIS states. I proceed here from the insight that "[f]inancial centers (…) are a bridge, an intermediate space, between the globalised part of finance and the thick national and local cultures of investment of a country or a region (Sassen 2012 p24). I examine how Riga was a node where global transaction banking meshed with the "thick national and local cultures" of the shadow economy of the CIS states, thereby "financialising the nonfinancial" in the form of the shadow economy (Sassen 2012 p24). This chapter examines the processes in Latvia from three perspectives: firstly, from that of the whitelisted onshore jurisdictions favoured by banks and their clients for registering shell firms. My argument is that within the Riga offshore assemblage, shell firms registered in a whitelisted, onshore jurisdiction replicate the whitelisting of Latvia as a banking jurisdiction explored in the previous chapter. Their legal structure replicates the offshore-onshore hybridity of the Riga assemblage.

Secondly, I examine Riga offshore banking from the perspective of its second most important market after Russia, Ukraine. Thirdly, I look inside the transaction pattern of a leading offshore bank. I attempt to place the Riga financial centre in a network of global money flows, in order to highlight its work mediating globalised finance and the local economic contexts. Triangulated together, these three perspectives present Latvia as a centre for the integration of the post-Soviet shadow economy into global banking, or put more plainly, a money-laundering centre.

7.2 Incorporating 'prestige': Shell firms in UK, New Zealand and US

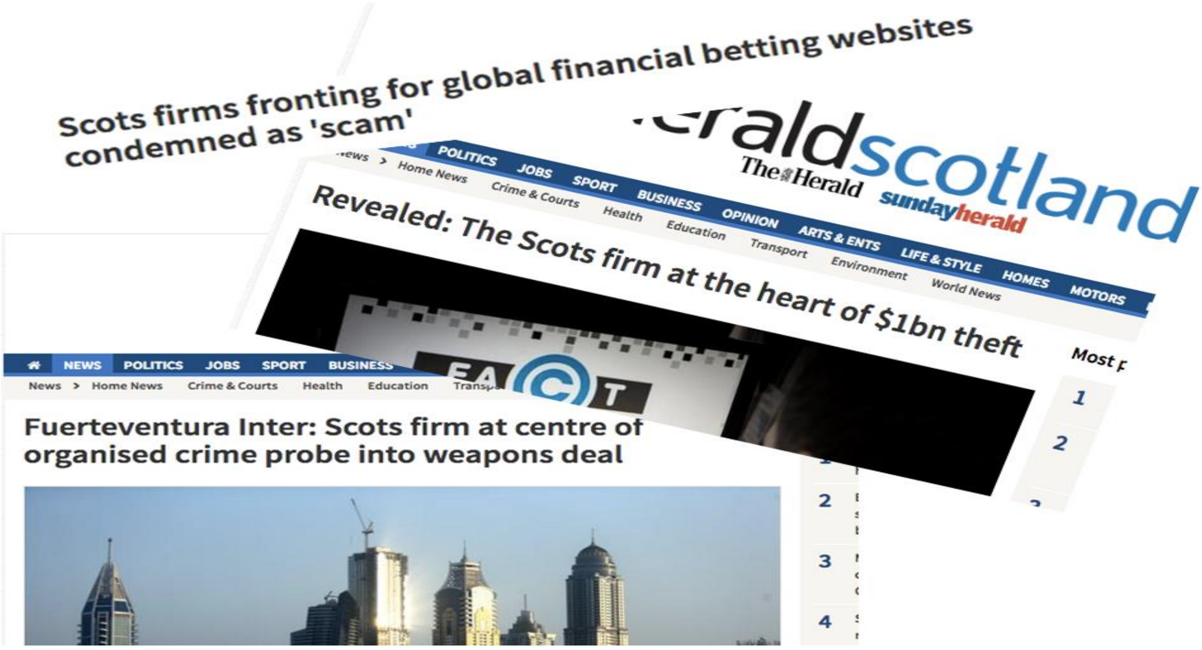
In 2015 Scotland was shocked to find itself in the midst of a major Eastern European bank fraud, which saw the equivalent of 20% of the GDP of Moldova siphoned out of the small former Soviet country in the form of fraudulent loans from a state bank. In November 2014, a Moldovan state-owned bank effectively disbursed over $1bn to local firms (Transparency 2017). After protests grew in Moldova, fueled by the suspicion that the organisers and beneficiaries of the fraud were among the country's government, the National Bank of Moldova commissioned a forensic audit of the loans. The audit showed that most of the $1bn had been transferred out of Moldova to around 20 Scottish shell firms (Transparency 2017, Kroll 2015). The unexpected role played by a raft of Scottish firms in a major corruption scheme in Eastern Europe, bearing the hallmarks of organized crime, prompted widespread media coverage and political responses in Scotland (BBC 2017a).

There followed a spate of money-laundering scandals involving Scottish firms (see Figure 9). The so-called 'Russian Laundromat' moved around $22bn out of Russia using Scottish shell firms and fake loans enforced in Moldovan courts. Other scandals involved Scottish firms in arms deals in Africa, unregulated web cash transfer systems, online gambling, etc. (DBEIS 2017). Almost all the stories had a connection to the former Soviet countries.

Adding to the feel of conspiracy was that many of these Scottish firms had the obscure legal form of a Scottish Limited Partnership (SLP). They were formed by a small number of company incorporation agents at a small number of addresses, with hundreds of partnerships registered at each address. Moreover, the partners forming the SLPs were offshore firms registered in tax havens such as Seychelles and Belize (Transparency 2017b). In response, the UK government launched a reform process for SLPs, declaring it "will do everything necessary to crack down on crime lords exploiting them [SLPs] to launder dirty money." (BBC 2018d)

Despite the public attention around Scottish LPs, few noticed that what was happening in Scotland had happened shortly before - in New Zealand. On December 11, 2009, Thai police at Bangkok Airport searched a Soviet-built cargo plane refuelling and found 35 tons of North Korean arms heading for Iran in breach of UN sanctions. The incident triggered alarm in New Zealand because the plane was leased by a New Zealand firm SP Trading, incorporated only weeks before and existing only on paper (Danssaert et al. 2009, Ryle 2011). The 'SP Trading case' shocked a country that, like Scotland, prided itself on its transparency only to be implicated a transaction that smacked of state-sponsored organized crime.

Figure 9. Collage of Scottish press headlines about shell firms 2014-2016



Source: www.scotsman.com, www.theherald.com

Also similar to Scotland, following on the 'SP Trading' case a succession of serious black-market deals using New Zealand firms added to the growing scandal (see Figure 10). As a New Zealand member of parliament summarized during a parliamentary debate in 2012:

> Hostas Ltd entered into government contracts with the Ukrainian Ministry of Healthcare. (…) Falcona Systems Ltd was allegedly used to gain $150 million in kickbacks for Ukrainian and Latvian officials (…) Tormex Ltd allegedly washed $680 million through bank account in Riga, Latvia. (…) Mexico's notorious Sinaloa drug cartel (…) used four New Zealand registered companies. (Companies and Limited Partnerships 2012)

As in Scotland, the firms implicated in the numerous scandals were incorporated at a handful of addresses without any physical presence. The Treasury department argued that the firms' purpose was "to create a confusing web of legal persons to launder money, traffic arms and illegal substances, and commit tax and other fraud" (The Treasury 2015). Like the Scottish scandal, government was forced to respond, finding that "people who wish to conduct unlawful activities overseas may increasingly seek to incorporate companies in New Zealand, in order to benefit from New Zealand's positive reputation. (…) the SP Trading case has become a very visible focus of such concerns (Ministry of Business Innovation and Employment 2011b p6). This led to the passing in 2014 of the Companies Amendment Act tightening up registration procedures.

Figure 10. Collage of New Zealand press headlines on shell firms 2009-201

Source: NZ Herald, Stuff.co.nz

The link between Latvian banks and shell firms in NZ and Scotland is well documented (FIU Latvia 2018, interviews #3 former UN arms control expert, #8 former AML officer in US Bank, #25 Latvian anti-corruption NGO investigator, #29 British AML officer). Latvia's second national risk assessment published in 2018 belatedly acknowledged that "a large number of shell companies established also in the EU, for instance, in Scotland, have been used" for large-scale money laundering via Latvian banks (FIU Latvia 2018 p32). Besides New Zealand, England & Wales and the US were at different times favoured sites of incorporation of shell firms. In 2005, 25% of Latvian non-resident bank deposits were held by US shell firms, until US protests forced this to change (see Chapter 8), prompting a shift to New Zealand and UK firms (FCMC 2005). Between 2005 and 2018, on average around 25% of Latvian bank non-resident customers were incorporated in onshore jurisdictions such as UK, USA and New Zealand, jurisdictions that are regarded as well-regulated (FCMC

2005, 2011, 2018). Such shell companies are often marketed as '*prestizhny'* or 'prestigious' to Russian-speaking business, and I use this epithet to denote them. There was a chronological succession starting with US shell firms until 2005-6, then England/Wales and NZ shell firms up to around 2012, after which SLPs predominated. In 2005, US shell firms held 25% of total Latvian non-resident deposits, in 2011, US, UK and New Zealand shell firms together held 20.1% of non-resident corporate deposits, and by 2018, 38% of shell firm clients of Latvian banks were from UK, of which many were Scottish (FCMC 2005. Figure 8, 9).

My argument is that these shell firms registered in a whitelisted, onshore jurisdiction such as Scotland and New Zealand replicate within the Riga banking assemblage the whitelisting of Latvia as a banking jurisdiction explored in Chapter 5. The onshore 'prestigious' shell firm is an important 'actant' within the offshore assemblage. The term 'actant' is used in Actor-Network Theory to refer to someone or something that has some form of agency, i.e. in its most basic sense something which can make things happen (Sayes 2014). "An actant can literally be anything provided it is granted to be the source of an action" (Latour 1996 p373). An actant has performative effects, whether it is human or not. In the context of my argument about money laundering as a performative referencing of the algorithm for clean money, the onshore shell firm incorporated in Scotland or New Zealand makes a performative claim to be clean, while protecting undeclared (shadow economy) funds.

These findings match those of Sharman that OCED countries are favoured sites of incorporation of shell firms used in money laundering (Sharman 2011). Sharman established that it was three times easier to set up an 'anonymous' shell firm, despite a clearly signalled intention to launder money, in OECD states such as UK, US, Australia, and Canada than it was in established tax havens (Sharman 2011 p126). Sharman connects the availability of anonymous shell firms in OECD countries to those countries' hypocritical reluctance to enforce at home onerous rules they force on poorer countries. However, I argue that shell firms in OECD countries are effective actants for money laundering because of the 'whitelisting' effect i.e. that shell firms incorporated in whitelisted jurisdictions such as UK and USA are more acceptable to banks, regulators and their screening software. Therefore, an infrastructure has emerged for incorporating such firms in these jurisdictions, as I discuss below in connection with 'business introducers'.

Investigators in the respective jurisdictions highlighted their country's reputation as the main reason for incorporation of the shell firms there. US investigators remarked on "the air of legitimacy afforded foreign owners in operating a U.S.-based company" (FinCEN 2006a). A Delaware Assistant Secretary of State official believed the state was "victims of our own renown" (Simpson 2004). A senior money-laundering compliance officer told Private Eye, in a report on the abuse of LLPs for laundering, that the UK "has the appearance of credibility, if you send your money through UK companies in and out of London, you have clean money" (Brooks and Bousfeld 2013 p20). New Zealand officials also believe believed that "New Zealand's positive reputation (…) may provide a veneer of legitimacy" to money launderers (MBIE 2011b p6).

While facilitating international payments by pretending to be onshore firms, 'prestigious' shell firms replicate the two main advantages of tax havens, freedom from tax and hidden ownership, leading their respective jurisdictions to be dubbed "tax havens the OECD forgot" (Unger and Ferwerda 2008 p32). Limited liability partnerships in the UK (also limited partnerships in Scotland) and limited liability companies in the US are tax transparent, i.e. it is the shareholders or members of the partnership who are liable for tax. Where the partners / owners are offshore firms, and the firm does no business in the onshore jurisdiction, such structures have no tax liabilities. At the same time, ownership is hidden. They are also cheap and quick to incorporate due to low administrative barriers (Unger and Ferwerda 2008, FinCEN 2006). It takes £12 and 12 minutes to incorporate a UK LLP (Companies House website).

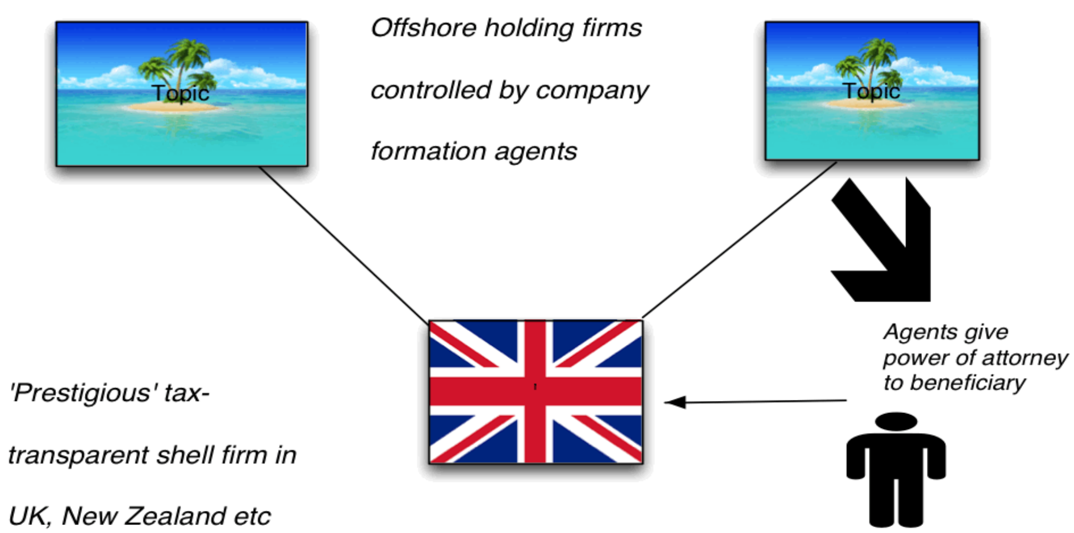
Table 19. Legal aspects of the 'prestigious' shell firm in USA, UK and New Zealand

Country	**USA**	**New Zealand**	**UK**	**Scotland**
Legal form	LLC	Ltd	LLP	LP
Tax	Pass through	Pass through	Pass through	Pass through
Ownership / partners	Hidden or nominees allowed	Nominees allowed	Foreign corporate partners and nominees allowed	Foreign corporate partners and nominees allowed
Ease of incorporation	Very easy	Very easy	Very easy	Very easy

Source: (Unger and Ferwerda 2008, Transparency 2017a, Transparency 2017b, Delna 2018, FinCEN 2006, New Zealand Treasury 2015)

The ‘prestige’ of such shell firms is thus a veneer as shown below, since offshore structures lurk behind the onshore facade (interview #29 British AML officer). This onshore-offshore hybridity replicates the onshore-offshore hybridity of the Latvian offshore assemblage argued above.

Figure 11. Onshore-offshore structure of ‘prestigious’ shell firm



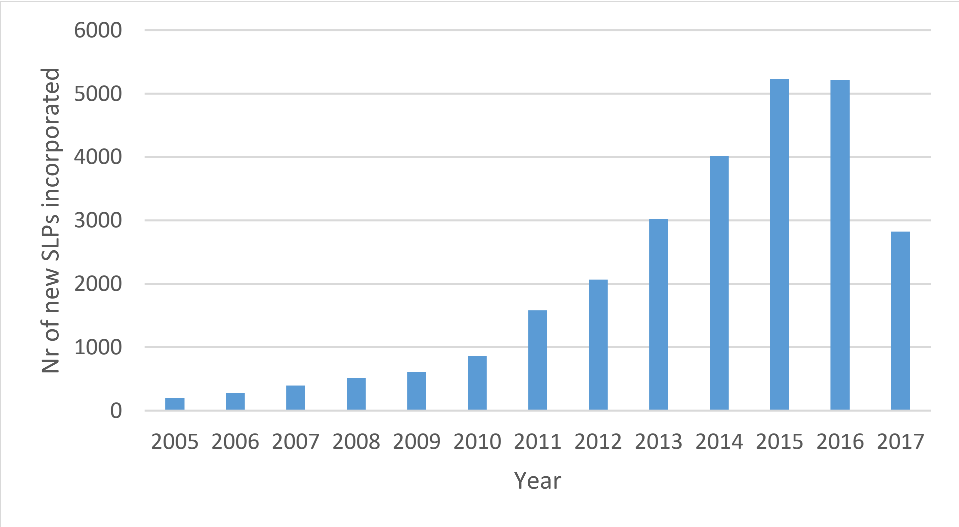
Source: (Unger and Ferwerda 2008, Transparency 2017a, Delna 2018, FinCEN 2006, Transparency 2017b, The Treasury 2015)

Sharman also neglects the role of banks as a force in the creation of shell firms in OECD countries. The public discussion in Scotland and New Zealand also omitted this aspect. Investigations show that these shell firms are incorporated for bank clients by ‘business introducer’ organisations themselves linked informally to Latvian banks (Delna 2018). This accounts for the conspiratorial clustering of firms at a handful of addresses discussed above. Business introducers organise a pipeline of shell firms for bank clients while handling their opening of bank accounts at Riga’s offshore banks, including customer checks (Delna 2018, Transparency 2017a, Transparency 2017b). They also act as marketing structures for the banks across the former CIS countries.

> [T]he majority of anonymous shell companies with Latvian bank accounts involved in illegal activity could be traced back to these agents. (…) In this way, corrupt networks were able to “bypass” customer identification checks, have access to the international financial system and avoid prosecution. (Delna 2018 p18)

These shadowy para-bank 'business introducers' are thus part of the assemblage of the Riga offshore sector. At the same time, they scout for new jurisdictions for mass incorporation of shell firms (Delna 2017, interviews #17 UK investigative journalist, #25 Latvian anti-corruption NGO investigators, #29 British AML officer). Thus the use of SLPs started after the UK Companies Act of 2006 (effective of 2008) required LLPs to have one human (non-corporate) director registered in the EU and after in 2010 New Zealand cracked down on shell firms. Numbers incorporated per year peaked in 2015-2016 until dropping in 2017 after reform measures in UK.

Figure 12. Number of new SLPs incorporated per year 2005-2017



Source: UK Companies House

Riga banks' mobilisation of these legal vehicles across different jurisdictions, designed by local affiliated para-bank structures, is - in a vastly different ethical-legal context - reminiscent of the nexus between advanced business services clustered in global financial centres such as London, global banks and the investment vehicles parked in offshore jurisdictions that ABS design and administer, as discussed in Chapter 2 (Wojcik 2013). This points to Riga also being a financial centre, but for shadow economy activities, as I explore in the next section.

Profiling the business activity of Scottish LPs by scraping web profiles

Because of this close link between offshore banking in Latvia and the SLP as a vehicle, it is possible to use SLPs as a proxy for Riga banks. In this section I profile the business activities of Scottish LPs established in 2015-2016 as a proxy for the offshore banks and their shadow economy activities. A web scraper ran an automated internet search for over 10,538 SLPs registered in 2015-2016, while filtering out redundant listings. Around 20% of all SLPs incorporated 2015-2016 had an identifiable online profile.

Table 20. Online business profile of Scottish LPs incorporated in 2015 and 2016

Category	2015	2016
Trading intermediaries for former Soviet countries	47.1%	41.7%
LPs with generic websites detailing broad trading profile, and no other traces	9.0%	14.2%
LPs linked to online business with high fraud risk (unregulated forex, crypto and binary trading, high-yield investment schemes, dating and mail order bride	8.10%	16.0%
Foreign shareholding or registration of foreign office	14.2%	7.33%
Legitimate online business (e.g. app developers, ecommerce, digital advertising)	13.9%	11.7%
Legitimate offshore business (e.g. transport and logistics)	5.44%	3.26%
Shelf firms and business introducers	2.21%	5.79%
Total firms with online profile	901	1105

Since a business profile could only be established for 20% of the SLPs, the breakdown is not representative, but the categories establish a profile of bank clients' business, albeit obviously weighted towards online business. Understanding SLPs as a proxy for Riga banks, the results point strongly towards CIS-linked shadow economy activities of as the predominant business of offshore banking in Latvia. In the following I highlight the links of the respective categories of business activity to post-Soviet shadow economy.

Trade intermediary is the leading business category among SLPs in 2015-16. Regarding shadow economy links, trade intermediary activities by shell firms have high risk of involving misinvoicing. Misinvoicing means that the prices paid by exporters or importers are altered by substituting an intermediary for the real foreign counterparty in order to alter the pricing of the deal with the aim of reducing customs and / or tax payments. Thus, the prevalence of trade intermediary operations is an indicator of high money laundering risks

(Eurasian Group 2009).

Of the trading intermediaries detailed above, only a handful have a company website identifying their activities. Conversely, another category I identified are generic dummy trading firms. These SLPs have primitive websites that describe in generic terms ostensible trading or consulting activity, without any external confirmation of this in trade databases, in contrast to the 'trade intermediary' category. These websites use google map plugins to falsely claim a real office location in Scotland. While these websites are unconvincing to the human eye, they may serve to satisfy automated checks on the SLP run by bank screening software. These websites are typically live only briefly and were retrieved using web archive or google cache. They suggest the respective SLPs are used to transit money using false trade documents ("konformashka") (see Figure 13).

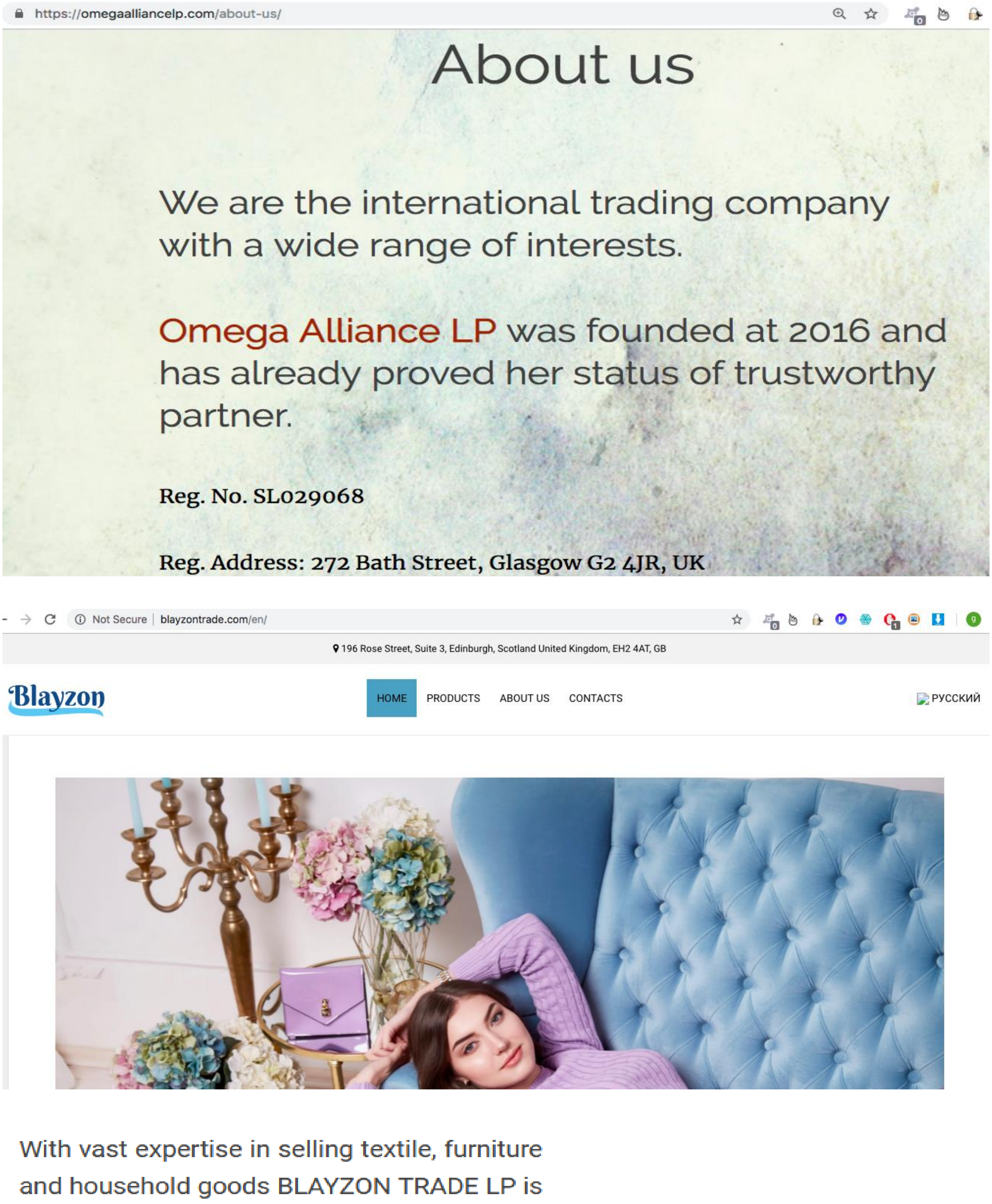
Fraud risks: Many SLPs were involved in unregulated online forex, cryptocurrency and binary option trading closely linked to pyramid schemes or other fraud. Such fraud schemes operating globally out of Eastern Europe have attracted law enforcement action in the US, Germany, Israel and Russia (Wells 2010, SEC 2018). As is the case with the generic trading websites discussed above, many such websites are only online briefly, hence the drop from 2016 to 2015

Legitimate business, online and offline: Legitimate online business encompasses app developers, web designers, ecommerce, and digital advertising. Most websites for SLPs involved in legitimate activities avoid identification of any persons, likely for tax avoidance reasons. Moreover, such business lines have less legitimate versions, such as malware apps or ad fraud widespread in digital advertising (Cyberscoop 2019, Buzzfeed 2019)

Genuinely 'offshore' activity' - shipping and logistics - account for around 5% of the SLPs traced online from 2015-2016. While there is a legitimate business model, payments from many illegal arms shipments have been processed by the Latvian offshore sector. (Wallace and Mesko 2013, interview #3 former UN arms control expert).

Business introducers A further 2%-6% of SLPs in 2015-2016 comprised business introducer's lists of incorporated shell firms for sale together with accounts at Baltic banks. As discussed, such business introducers act as marketing divisions for the banks.

Figure 13. Screenshots from generic websites of Scottish LPs



Source: www.omegaalliancelp.com www.blayzontrade.com, date: 14th December 2018

7.3 ‘Prestigious’ shell firms and the ‘laundromat’ business model

The integration of the post-Soviet shadow economy into US correspondent banking analysed in Chapter 5, continued post-2000 being routed mostly via Riga, and using the ‘prestigious’ shell firms registered in US, NZ and UK. Post-2000 the expansion of the global transaction business outlined in Chapter 5 continued, as secure internet technologies allowed remote banking by clients to become the norm. Daily payments made via the SWIFT system reached $5.5 trillion in 2005, and $7.7 trillion by 2011 (Scott and Zachariadis 2014). Following the global financial crisis of 2008, global banks relied all the more on transaction business as a “safe haven” providing stable revenue.

> In September 2013, the head of global transactions of a leading global bank shared with the author his assessment of the importance of correspondent banking, with respect to the effects of the latest financial crisis: “Citigroup would be gone without correspondent banking.” (Guttenberg 2019 p61-62)

Post-crisis, the global payments systems remained dominated by SWIFT, in turn governed largely by the same global banks that had triggered the financial crash in 2008 (Dörry et al 2018). Banks’ transaction business grew to reach 34% of bank revenues in 2016, revenues from implementing cross-border payments, forex transactions and trade services reached $145bn (Dörry et al 2018).

The marriage of dollar correspondent banking and the CIS shadow economy as described for the 1990s in Chapter 5 continued post-2000 in the form of the Latvian offshore banking assemblage. As described for the 1990s, ‘laundromats’ were the form this marriage took. The ‘prestigious’ shell firms in US, UK and NZ became one of the building blocks of such laundromats. Transparency International defines ‘Laundromat’ operations in the context of UK shell firms thus: “[C]omplex money laundering schemes that are used over multiple years, involve thousands of companies, and use tens of thousands of transactions to ‘layer’ funds into the global financial system” (Transparency 2017a p29). Laundromats are operated predominantly via Baltic offshore banks with US correspondent accounts (Transparency 2017a). My fuller definition is that a ‘Laundromat’ comprises: a network of international shell firms controlled by operators, who move pools of clients’ undeclared money through them using falsified documentation (fake invoices and contracts) in a large number of transactions designed to obscure traces, before making payments to beneficiary accounts according to the clients' original requests (to personal bank accounts, to importers, for luxury consumption articles etc). According to a Council of Europe investigator, a Laundromat has the following payment pattern:

> Money is channelled via different bank accounts and different banks. Very very quickly. And the point (…) is that by doing so, by having multiple transactions with the same funds, you are not able as a government to trace this siphoning off of the funds via these different bank accounts. Very quickly moving the funds around the world to a destination (…) the laundromat is in fact it is not only the tumbling of the money in the machine but it is also (…) the process whereby you lose track as a government of where the money flows through. So it ends up, it pops up somewhere in the UK for example or the British Virgin Islands. But the money is held in a Swiss bank account and held by that company offshore. [interview #11 Council of Europe investigator]

An investigative journalist described the possible final destination of funds moved through the 'laundromat' as "an account in Switzerland or to buy a house in Spain, or to buy goods in China" [interview #13 European investigative journalist].

Notably, these descriptions match those of the BoNY scheme and its euphemistically named 'global custody system' from the 1990s, as discussed in Chapter 5: a "complex web of hundreds of offshore companies" designed to "evade payment of Russian taxes and duties, and provided the ability to launder proceeds from illegal acts" (BoNY Derivative Litigation Case). The term 'Laundromat', while referencing money laundering, also references what in the BoNY case was called '*prokrutki'* - the 'spinning' of money through numerous shell firms via multiple redundant transactions, which journalists now dub the 'spin cycle' of the Laundromat (interview #13). In the CIS space, such a 'laundromat' was often termed in Russian a 'platform' (interview #13 European investigative journalist, interview #7 former Ukrainian banker, interview #10 former Latvian financial market regulator). Thus, like the BoNY case in the 1990s, the 'laundromat' model was a marriage of transaction banking (high speed high volume international electronic fund transfers) with shadow economy elements (undeclared funds and informal institutionalisation). The difference to BoNY's 'global custody system' is that following the political exposure of 1998-2000, the laundromat scheme was facilitated by the centrality of Latvia, as a whitelisted financial centre that US correspondent banks continued to work with after mostly withdrawing from Russia.

After the 1990s, Laundromat payment patterns via prestigious shell firms are strongly associated with Baltic banks. Between 2000 and 2006, US authorities were aware of how US shell firms were being used in such operations linked to Eastern Europe (GAO 2000). An initial probe in 2000 developed into a full report in 2006, concluding that: “The use of domestic shell companies as parties in international wire transfers allows for the movement of billions of dollars internationally by unknown beneficial owners. This could facilitate money laundering or terrorist financing” (FinCEN 2006 p2). The activity involved U.S. shell company accounts at Latvian and other post-Soviet banks transferring funds for pyramid schemes, stock market fraud, telecoms fraud, and corruption (FinCEN 2006). The funds went to “an unusually wide variety of beneficiaries in many locations,” frequently registered in tax havens. Payments were in bursts of high frequency, and either did not reference goods or services or referenced “remarkably dissimilar” goods and services, ranging from computers and footwear to steel and meat products for the same firm (FinCEN 2006 p12, Simpson 2004).

The payment pattern of UK and NZ shell firms seen at a US correspondent bank 2006-2009 was of a large number of dollar payments to beneficiaries all over the world, with apparent ‘smurfing’. ‘Smurfing,’ a reference to the well-known miniature cartoon characters, denotes breaking up large sums into a series of smaller payments, each under the threshold value triggering enhanced monitoring. Many payments went and were received from other shell firms banking out of Riga, with money flowing from the shell firms to wealth accounts in Switzerland and as payment for imports from China at the top of the list [interview #8 former AML officer in US bank]. A Reuters investigation into UK shell firms at that time analysed $2bn in similarly structured dollar transactions involving UK shell firms. (Bergin and Grey 2016)

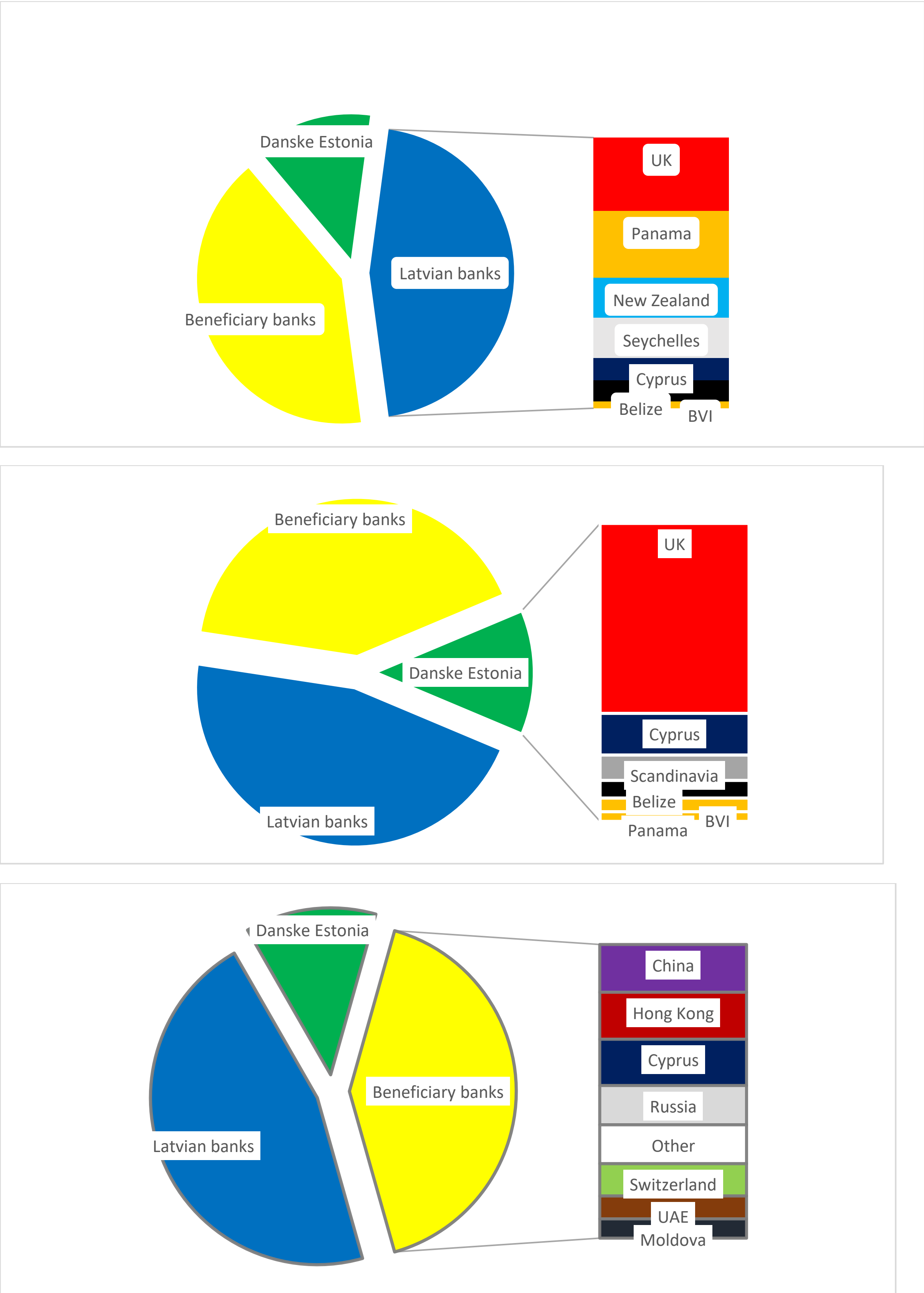
Transparency International UK (TIUK) constructed a database of 766 UK shell firms implicated in money laundering episodes in open sources, drawing on journalist investigations (Transparency 2017a). “The laundromats were used by politicians, public officials and organized criminal groups, as well as businesses for embezzling funds, disguising the origins of money, evading taxes or sanctions, paying bribes, bypassing customs fees or legitimately moving funds from high corruption risk environments to ‘safe haven markets’ (Transparency 2017a p29), Almost all had Baltic bank accounts, mostly in

Latvia but also at one Estonian bank, Danske Bank Estonia, discussed below. (Transparency 2017a p29).

According to a series of investigations by Organised Crime and Corruption Reporting Project (OCCRP), in one episode around $20bn in undeclared money was moved out of Russia via a Latvian bank using a series of shell firms, many of which were incorporated in Scotland. Much of the money went ultimately to offshore financial centres such as Switzerland, but also to China, apparently as part of customs fraud, whereby importers to Russia understate the price of goods they are importing to customs authorities in order to reduce their customs payments. (OCCRP 2014b) They then paid the balance due to the Chinese counterparts off-the-books using laundromat-type services (interview #7 former Ukrainian banker, #10 former Latvian financial market regulator).

Figure 14 shows the three paths that $15bn in undeclared money moved out of Russia via the 'Russian Laundromat' took after arriving in Latvia onto several 'core accounts' in Latvian bank Trasta Komercbanka. From these core accounts, around $6.5bn was paid to further shell firm accounts in Latvia registered in UK, Panama, NZ, Seychelles, Cyprus, Belize and BVI, from whence it likely moved further onto beneficiary accounts. Around $1.5bn was paid to similar shell firm accounts at Danske Bank Estonia, a bank which thanks to a whistleblower, media coverage and an independent investigation has become a byword for money laundering (Bendtsen et al 2019) Danske Bank Estonia department for non-residents was highly networked with the Riga assemblage, both infrastructurally, served by the same 'business introducers' and financially (OCCRP 2020, 2021). Thus the Danske Bank Estonia case can be regarded as a halfway position between BoNY's Eastern European department in the 1990s, where a department of a US bank was directly enmeshed with the CIS shadow economy, and the Latvian case, where an entire offshore banking sector was politically networked with "Western civilisation" and whitelisted while simultaneously enmeshed with the CIS shadow economy. Danske Bank Estonia lacked the political protection in Estonia that the Latvian offshore sector enjoyed, but its integration as a unit of a respected Western

Figure 14. Path of $20bn after initial core companies of 'Russian Laundromat'



Source: OCCRP

European bank compensated for this (Bendtsen et al 2019). The BoNY and Danske Bank Estonia cases resulted in independent investigations, because ultimately, albeit belatedly, the introduction into the US financial system of banking units enmeshed in the CIS shadow economy triggered red flags and whistleblowers. As I describe in the next chapter, the Latvian case ended in a foreign policy debacle for Latvia in 2018, not no domestic investigation because of the extent of political protection of the sector in Latvia.

The largest part of the 'Russian laundromat' money, $7bn, was paid directly to beneficiary – i.e. final recipient - accounts at banks in China and Hong Kong, Cyprus and Switzerland, UAE, and Russia and Moldova, as shown in Figure 14. It is important to note that in such 'laundromat' cases, the operators are moving the undeclared funds of third parties - their clients - through the system of shell firms with Baltic bank accounts, until paying the money out to the beneficiary account in Switzerland, China or elsewhere as requested by their client (interview #7 former Ukrainian banker). Thus, there is a strong informal institutionalisation of the scheme, because the CIS originators of the money have no legal recourse to reclaim their funds, should they be diverted by the operators of the 'laundromat' (Fituni 2000, Ledeneva 2000). Such a high level of informal institutionalization as manifest in Laundromats is one of the salient features of Latvian offshore banking (Delna 2018)

This informal institutionalisation of transactions totalling billions of dollars per day is remarkable. The Riga-centred laundromat system can thus be compared with an informal value transfer system, also known as alternative payment system, albeit one mounted on the formal global dollar payments system. Other examples of informal payment systems arise in particular in the Islamic world, as discussed in Chapter 3, in the form of Hawala, Hundi and Fei-chien etc (Gilligan 2001, Ballard 2003). Such alternative payment systems are associated with 'archaic' practices, but in reality thrive in the modern world, in the context of new communications such as the Internet, and interlinked with the conventional financial sector. Geographers describe the 'interwoven' relationship between Islamic finance [underground banking] and 'conventional' finance (Pollard and Samers 2007).

> The two key features of underground banking are remittance and trust. (…) As we shall see, the traditional characteristics of underground banking of the slow old world are well suited to the super fast era of late-modern capitalism." (Gilligan 2001 p106).

The Riga example can thus help to 'de-orientalise' the discussion of alternative payment systems by highlighting their links to the formal financial sphere, and thus their being situated in the contemporary global economy rather than the 'exotic East' (De Goede 2012, Pollard and Samers 2007, Razavy and Haggerty 2009).

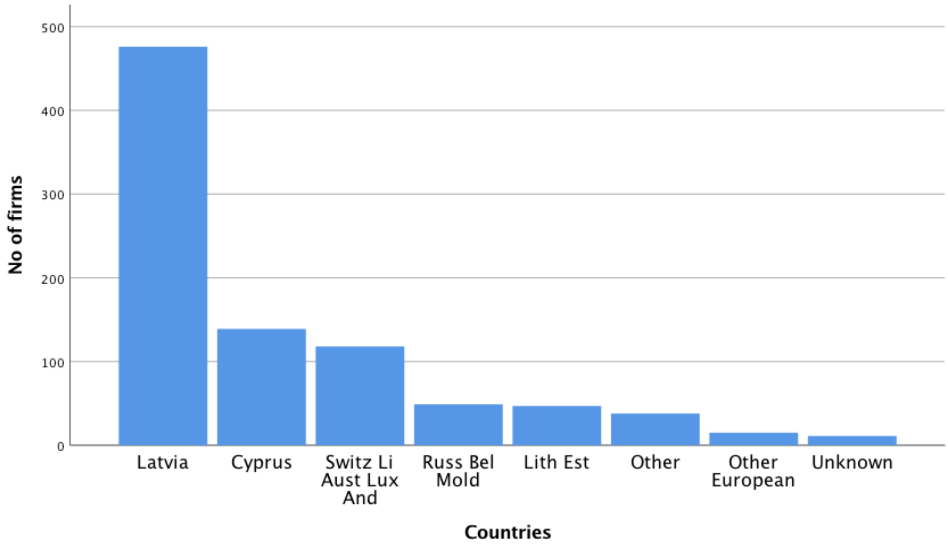
7.4 Mapping the role of Latvian banks in the shadow economy in Ukraine

In this section, I focus on Ukraine, the second largest CIS state after Russia. The focus on Ukraine helps understand Riga as a shadow-economy OFC for the CIS states as a whole, rather than merely an adjunct to Russia. Quantifying the role played by Latvian banks in Ukrainian shadow-economy transactions may indicate the overall role of Latvian banks in the CIS shadow economy.

I draw on Ukraine's Unified State Register of Court Decisions (USRCD) to assess Latvian banks' involvement in the shadow economy in Ukraine, which I operationalise as the involvement of clients of Riga banks in economic crime in Ukraine. I identified 213 economic crime investigations involving foreign banks over the last ten years in Ukraine's USRCD. Almost all of these involve use not only of banks, but also of shell firms in countries outside of Ukraine. The results show that Latvian banks were part of the financial institutionalisation of the shadow economy in Ukraine. 155 of these cases involve Riga banks exclusively or in combination with banks from other countries. Over half of the firms involved in economic crime in Ukraine banked in Latvia (482 out of 961). The fact that Latvia's offshore banks are so frequently implicated in Ukrainian economic crime investigations points to Riga's offshore banks operating as a shadow-economy financial centre.

Profiling the Latvian-bank clients involved in economic crime in Ukraine can also shed light on the relationship between these 'criminal' clients and the overall Riga bank clientele. Using the data from the USRCD, it was possible to profile Riga bank clients by country of incorporation (domicile) and the specific Latvian bank used, as shown in Figures 15 and 16 respectively. Notably, the distribution of 'criminal' clients in Ukraine by domicile roughly follows the overall distribution of clients of Riga banks by domicile. This suggests that the profile of 'criminal' clients of Latvian banks in Ukraine is not noticeably different from the overall profile of Latvian bank clients.

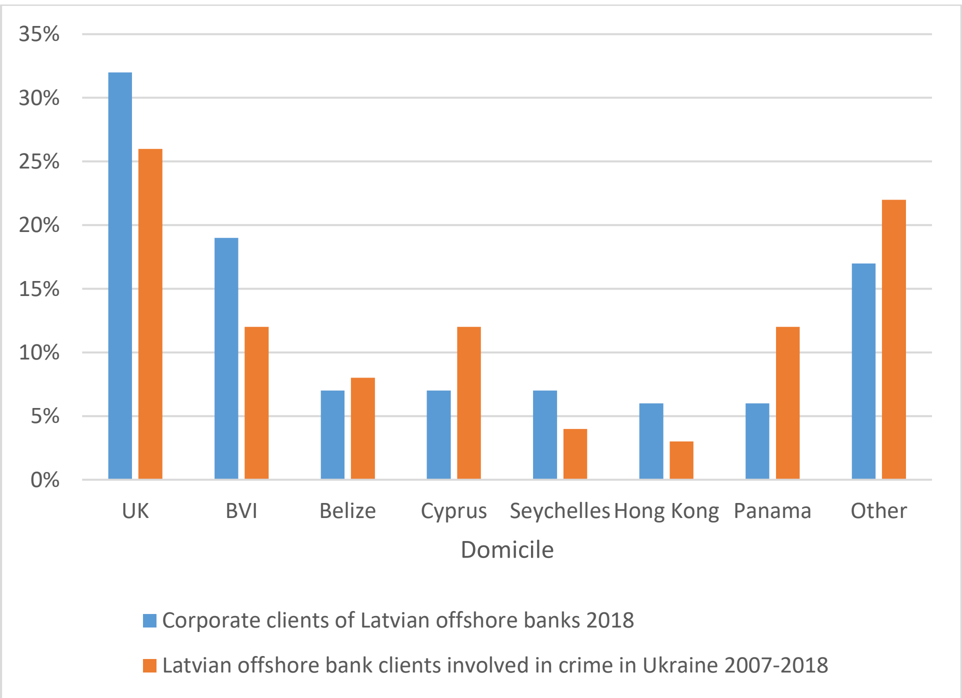
Figure 15. Countries where firms involved in economic crimes in Ukraine bank



Key: Switz = Switzerland; Li = Liechtenstein; Lux = Luxembourg; Aust = Austria; And = Andorra, Russ = Russia; Bel = Belarus; Mold = Moldova; Lith=Lithuania; Est = Estonia

Source: USRCD

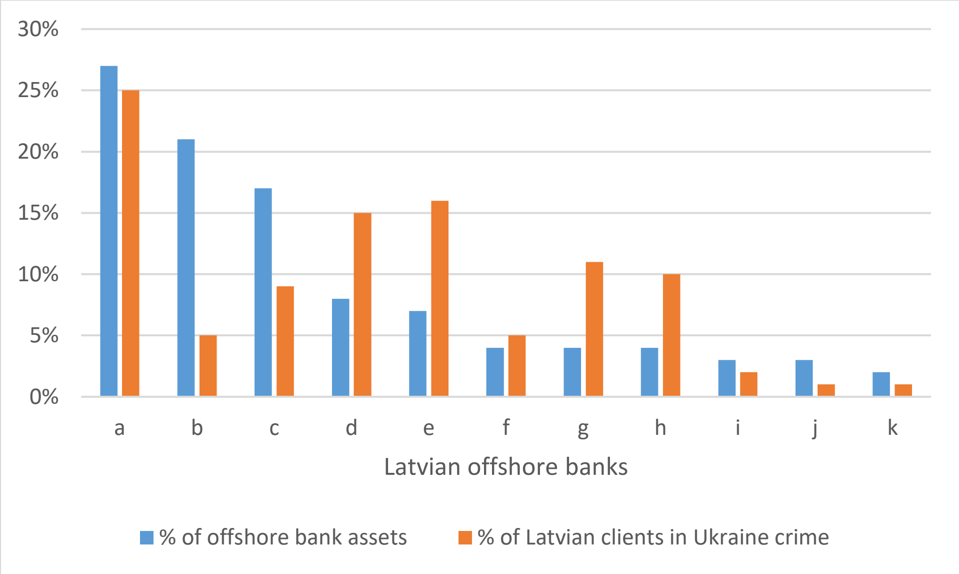
Figure 16. Domicile of clients of Latvian offshore banks cf. those involved in economic crime in Ukraine



Source: USRCD

Similarly, Figure 17 shows that the distribution of 'criminal' clients of Latvian banks in Ukraine, when profiled by the specific Latvian bank used, does not strongly differ from the overall profile of Latvian bank size by assets, except in ways that can be explained by the Ukrainian market.

Figure 17. Latvian offshore banks by size cf number of 'criminal' clients in Ukraine

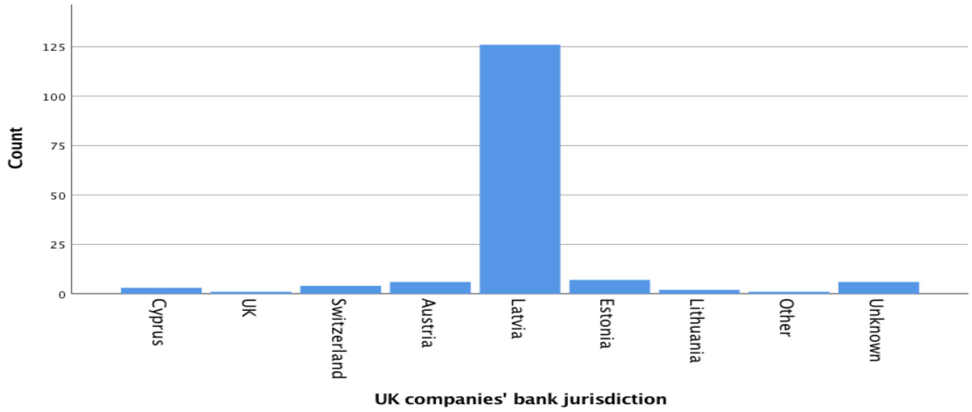


Source: USRCD

The biggest discrepancy is the low number of clients of bank 'b' involved in economic crime in Ukraine, compared to its place as second largest offshore bank by assets. This can be explained because bank 'b' was not active on the Ukrainian market [interview #24 former Latvian banker]. The high number of clients of banks 'd', 'e', 'g' and 'h' involved in crime in Ukraine can be explained by these banks being subsidiaries of Ukrainian banks or having major Ukrainian shareholders. Therefore, overall, there is little to strongly distinguish the clients of Riga banks involved in crime in Ukraine from the overall profile of clients of Riga banks. This supports the argument that Latvia's offshore banking sector as a whole was the exporter of money laundering services, i.e. a money laundering hub for the CIS market.

Almost all UK firms named in criminal investigations in Ukraine, banked in Latvia, confirming 'prestigious' shell firms as characteristic of Riga offshore banking.

Figure 18. Countries where UK firms listed in Ukrainian criminal investigations bank

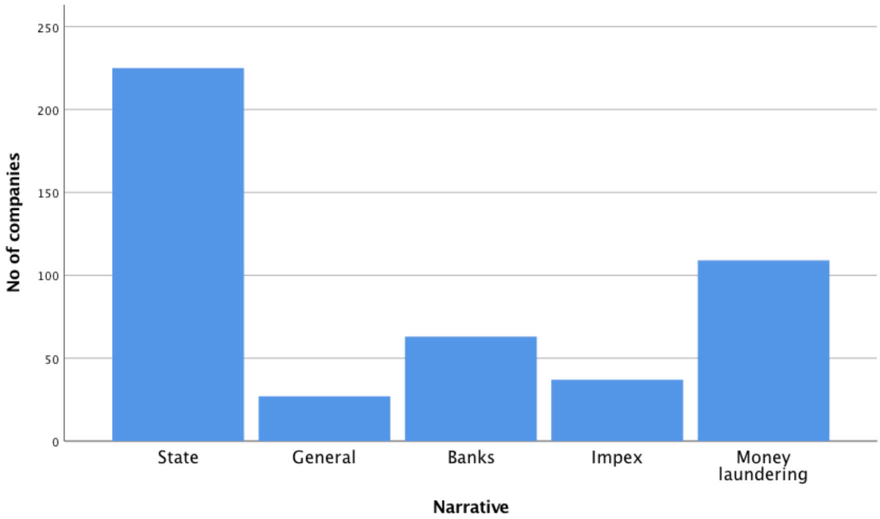


Source: USRCD

125 of the 177 UK firms listed in economic crime investigations bank in Latvia. Of these, 43 are SLPs and 68 are LLPs registered in England and Wales. The remaining 66 firms were limited companies. While thus comprising two-thirds of the 'criminal' UK firms in Ukraine, limited partnerships are a rare phenomenon in the UK, comprising only 1.58% of all companies incorporated in the UK (Transparency 2017a). This shows how not just how UK as a jurisdiction, but specific rare UK legal forms have been adapted for use by Latvian bank clients, as discussed above.

The data for the Latvian banks contained in Ukraine's court register highlights the political embeddedness of the Riga offshore sector in the post-Soviet countries. Thus, the most prevalent crime narrative for firms banking in Riga is political corruption, with over 200 shell firms banking in Latvia named in connection with corruption cases in Ukraine, double the number for the next most frequent crime narrative, money laundering.

Figure 19. Ukrainian economic crime narratives for firms banking in Latvia

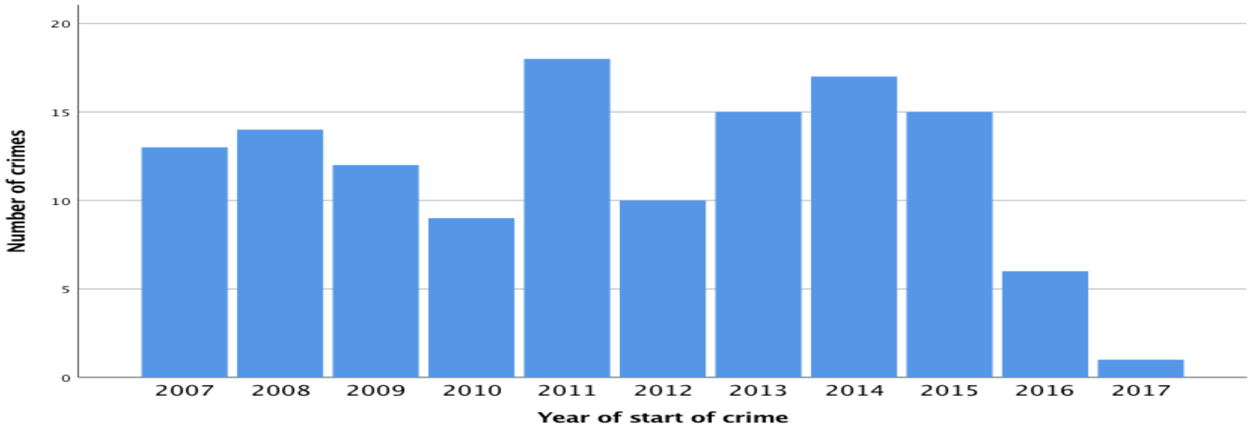


Source: USRCD

Political corruption thus appears to be a strong business line for Riga banks. However, in terms of total amount of money, money-laundering cases are in first place, according to analysis of the USRCD. This is because money-laundering cases often refer to 'laundromat' type schemes, including the widespread 'black cash' tax evasion schemes discussed in Chapter 5, estimated at billions of dollars per year. Thus, they represent part of Ukraine's shadow financial institutionalisation, and thus indirectly include revenues from political corruption, as well as from other sources, such as the largescale VAT evasion operations known in Ukraine as 'conversion centres,' which are an interface between the banking system and 'black cash'. Secret funds moved out of Ukraine via Latvia may have originally been paid by customers to operators in cash, while offshore funds moved into the country may likewise be 'converted' to cash and paid out locally to customers. "Moving funds offshore and moving them onshore with subsequent conversion to cash for the purpose of breaking the chain" is "one of the biggest current problems in the economy," according to Ukraine's state financial monitoring service (DSFMU 2012 p36).

The high level of bank fraud in Ukraine involving Latvian banks also points to their role in institutionalisation of Ukraine's shadow economy. Such bank fraud cases in Ukraine usually involve fraud committed by the bankers themselves against their banks, such as fraudulent insider lending, also known as siphoning of funds. Such cases can run to hundreds of millions and even billions of dollars, as was the case with Ukraine's largest bank Privatbank, which had to be nationalised in 2016 as a result (FT 2020). The close connection of Riga banks to both the political and financial systems in Ukraine, makes it possible to speak of it as being part of the infrastructure of the shadow economy in Ukraine. Notably, the role of Riga in Ukraine remained mostly constant over the period examined 2007-2017, despite two changes of power in 2010 and 2014 respectively, the latter via revolution.

Figure 20. Number of crimes per year linked to Latvian banks



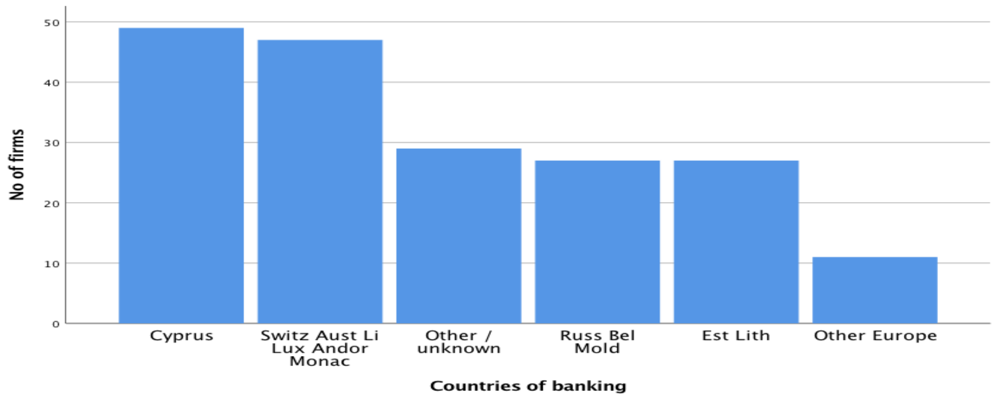
Source: USRCD

The tail-off for 2016 and 2017 likely reflects a time lag between crime and investigation, although international pressure on Latvian banks discussed in Chapter 8 may also have taken effect.

Analysis of the destination of the money moved out of Ukraine via Latvia shows a number of banking jurisdictions associated with Riga offshore banking frequently appearing in criminal investigations together with clients of Latvian banks. These jurisdictions associated with Riga fall into three categories: European offshore banking centres - Switzerland, Austria, Liechtenstein, Luxembourg, Andorra, and Monaco. As we shall see in the case studies below, where Ukrainian criminal investigations of political corruption name a beneficiary account as the final destination of illicit funds moved out of Ukraine by politicians, it is usually in these countries.

The second group are other transit jurisdictions such as fellow Baltic countries Estonia and Lithuania, as discussed above. Cyprus comprises a hybrid form, partly as jurisdiction for beneficiary accounts before the 2013 Euro crisis, but latterly arguably more a transit jurisdiction. The third group comprise other originator countries like Ukraine from the CIS, Belarus, Moldova and Russia. Some money from these countries passes Ukraine on its way to Riga. There are also a number of isolated cases of illicit funds being moved to Russia from Ukraine, but these constitute an exception. Analysis of Ukraine's USRCD shows that dirty money moves westwards, not eastwards. However, despite frequent allegations of the City of London being used to launder dirty money from Eastern Europe, such cases are rare in cases examined in the USRCD, despite the frequent (deceptive) use of UK firms. Instead, dirty money flows via Riga to the classic European offshore finance states, Switzerland, Cyprus, Austria, Liechtenstein, Luxembourg, Andorra and Monaco.

Figure 21. Jurisdictions associated with Latvian banks in Ukrainian criminal cases



Key: Switz = Switzerland; Li = Liechtenstein; Lux = Luxembourg; Aust = Austria; And = Andorra, Russ = Russia; Bel = Belarus; Mold = Moldova; Lith=Lithuania; Est = Estonia Source: USRCD

Focus on political cases

The following cases shown in Table 21 are intended to make more concrete the different modalities of Riga banks' role in Ukrainian political corruption based on the USRCD, and thus to illustrate the role played by shell firms as 'actants' in the Riga assemblage, and the damage inflicted on the societies of the CIS thereby.

I group cases into four categories, according to the level of detail available on the passage of money, and the different modalities this detail reveals. The first group concerns direct transfer of embezzled funds to shell firms with accounts in Latvia. In the second group, embezzled funds move first to local or foreign companies, before being moved to Riga. In the third group, money moves via Latvia to beneficiary accounts for instance in Switzerland, or to acquire luxury real estate, for instance in Croatia. The fourth group includes cases where funds return to Ukraine from beneficiary accounts in Europe to acquire real estate or otherwise used in Ukraine.

Table 21 shows how damaging the activities of Latvian offshore banking was to Ukraine, one of its major markets. Analysis of the USRCD thus shows how money laundering by Latvian offshore banks and thus the ineffectiveness of AML in Latvia's offshore sector impacted on the target markets. This highlights how money laundering activities by Latvian offshore banks comprised the export of financial services, i.e. money laundering, to foreign markets. Therefore, Latvia was a dominant player on one part of the global money laundering market, as conceptualised by Gnutzmann, McCarthy and Unger:

> Laundering is a globally traded service: capturing the idea that a single broken link in a financial transaction is enough to break the chain of accountability associated with a transaction. (Gnutzmann et al 2009 p247)

According to Gnutzmann et al, small countries may adopt a lax or even tolerant approach to money laundering in order to compete on the global ML market, since the financial gains from doing so in small developing or transition economies outweigh the potential negative domestic effects. Small countries may thus "dance with the devil" by exporting money laundering services: "for small countries, laundering is especially cheap to produce (…) because the costs caused by increased crime are borne almost entirely by other countries" (Gnutzmann et al 2009 p245). Gnutzmann et al argue that such a "defection" from AML by a small country, leading to export of money laundering services, "is largely determined by government policy" of either lack of AML laws or their weak enforcement (Gnutzmann et al 2009 p247). As argued in Chapter 6, and reprised in the next chapter, Latvia had an informal strategy of ringfencing the offshore banking sector from full application of AML regulations, which one of the key factors in the international competitivity of the sector, and its dominant role on the money laundering market in Ukraine. Its money laundering effectiveness can be seen in that in few of the cases in Table 21 could investigators follow the money trail from Ukraine to the beneficiary accounts, for instance in Switzerland, pointing to the weakness of the anti-kleptocracy regime described by Sharman (Sharman 2017).

Table 21. Ukrainian criminal investigations of corruption involving Latvian bank customers

All shell firms bank at Latvian banks, unless otherwise stated. All cases are investigations on suspicions of embezzlement.

1) State official or state company does direct corrupt deal with shell firm banking in Riga which acts as an intermediary in a deal or supplier of fictitious goods or services (such as consulting (16 cases)

Year	Amount	Narrative and investigation number (Nr.)
2008	$11.4mn	A state arms trader paid a UK shell firm ostensibly for lobbying work in Kazakhstan. Nr. 22014220000000000
2009-2011	$1mn	State officials implementing the court decision database used UK shell firm to receive payments from private local IT contractors. Nr.12012000000000007
2010-2014	$46mn	In 2010-2014 a state arms exporter paid diverse shell firms ostensibly for lobbying in Iraq Nr. 42013000000000300
2011-2014	n/a	State forestry agency officials sold timber off-the-books to BVI and Scottish shell firms Nr. 12013110000000300
2010-2014	n/a	State forestry agency head investigated over connections to offshores. Nr. 42016000000002900
2011-2013	n/a	Officials in the state architecture inspection permitted construction of a helicopter landing platform owned by UK shell firm at a protected site in Kyiv. Nr. 42016000000002900
2012-2015	$7.5mn	State chemical research institute paid shell firms in Uruguay and UK ostensibly for goods and services. Nr. 12016040000000015
2013-2015	$3mn	State defence plant officials paid an SLP ostensibly as sales agent. Nr.52016000000000400
2014	$0.67mn	State grain trader officials sold grain cheaply to Cyprus firms they controlled. Nr. 42017000000001000
2011	n/a	State forestry agency officials received kickbacks paid to shell firms in Panama, New Zealand, and UK. Nr. 52016000000000400
2015	$144,000	State defence plant managers received money from Armenian contractor paid to UK, Nevis and Belize shell firms. Nr. 52016000000000400
2013	n/a	State grain trader officials embezzled some of $1.5bn loan from China using a Swiss firm and a Belize firm as counter-parties for contracts Nr. 42014000000000200
2015	$2mn	State chemicals firm officials sold products to UK shell firm at below market price. Nr. 42015160000000300

(Table 21 continued)

2014-2015	n/a	State company officials used a UK shell firm as intermediary when contracting surveyance work on a chemicals pipeline at markup. The UK shell firm then hired a local firm for the work Nr. 42015000000001900
2015	n/a	Kyiv region customs officials used two UK shell firms to handle bribe payments from importers. Nr. 42016100000000300
2016	$7mn	Odesa city officials bought real estate for municipal needs at inflated prices from an SLP and local firms. Nr. 5201600000000411

2) State officials divert money from the state organisations via domestic or foreign companies. In a second step, the money is moved from the first receivers to shell firms banking in Riga (14 cases)

2009-2012	n/a	Czech engineering company paid bribes to Ukraine MP for sales to Ukraine's state nuclear power company, some of which were moved from French and Swiss accounts through a series of shell firms with Latvian accounts back to Ukraine. Nr. 42014000000000029
2009	$8mn	Ukraine's health ministry paid Ukraine supplier above-market price for influenza vaccine it purchased from US shell firm as intermediary. Nr. 12014000000000518
2011	$160mn	State energy company officials purchased a drilling rig from a Latvian shipyard, which in turn acquired it from a UK shell firm, at a markup of $160mn, $50mn of which was paid to a small Turkish firm. Nr. 42014000000000000
2009-2013	$120mn	State energy company lost over $120mn due to off-the-books sales of compressed gas to local firms, with revenues subsequently moved through UK, Panama and other shell firms Nr. 42014000000000400
2011	$30mn	State funds intended for modernisation of Odesa airport diverted from local firm to UK shell firm ostensibly for equipment purchase Nr.52016000000000214
2011	€3.9mn	Natural resources ministry paid an Austrian firm ostensibly for software from an Austrian firm, the money then passed through a UK firm with Cyprus bank account to two Belize firms with Latvian accounts. Nr. 42014000000000181
2011-2013	$30mn	Head of National Bank of Ukraine (NBU) and government minister set up an NBU TV channel used to siphon money to shell firms in BVI and UK. Nr. 42014000000000300
2013-2016	$100mn	Local firms with joint production agreements with state gas producer understated the gas produced by around $100mn, revenues siphoned to Cyprus and UK shell firms that owned the local firms. Nr. 52015000000000002

(Table 21 continued)

2014-2016	$13.1mn	Officials at state titanium miner sold ore at reduced price to intermediaries in Austria (Austrian account) and UK (Latvian account). Nr. 42017100000001392
2013	$0.9mn	State nuclear power company purchased an operating system from a Ukrainian firm for $1.5mn, the Ukrainian firm acquired it from a Latvian intermediary controlled by officials, which bought it from the Russian producer for $0.6mn. Nr. 42015000000001300
2013-2015	€0.7mn	Officers at state explosives plant used a UK shell firm as intermediary to buy detonator parts from a Czech producer at a €0.2mn markup. Nr. 42015040000000056
2014	$15mn	State grain trader officials overpaid to acquire a local stevedore company from a Cyprus shell firm Nr. 32016220000000100
2014	$60mn	State grain trader officials company caused losses of over $60mn to the company when payment a Saudi Arabia counterparty paid a BVI shell firm for a grain shipment instead of the state company. Nr. 52017000000000070
2014	$3mn	Health ministry officials embezzled budget funds when purchasing vaccines from local supplier, which failed to deliver but transferred funds to a UK shell firm. Nr. 12015100000000500

3) Stolen funds are moved via shell firms banking in Latvia to private beneficiary accounts in Switzerland, Austria, Cyprus, Liechtenstein, Luxembourg, Monaco etc or moved abroad to via shell firms to buy real estate etc (9 cases)

2009-2012	$37.5mn	An MP embezzled $37.5mn from a bank under temporary administration by forging documents ordering payment to a local law firm. The money was withdrawn as cash, and transferred out of the country via a UK shell firm, then to a BVI firm with Swiss bank account. $16mn was spent to acquire a private jet. Nr. 12013000000000500
2010	$58mn	Odesa regional officials inflated the cost of construction work by local firms, some of the money was moved to a NZ shell firm, then paid to Monaco bank accounts. Nr. 42014160000000101
2011-2014	$770mn	An MP embezzled state funds, including money paid to a state company under the Kyoto Protocol, transferred to domestic shell firms, then moved BVI, UK, Singapore and Cyprus shell firms, some used to buy real estate and open accounts in Monaco, where the MP now resides. Nr. 42014000000000029
2011-2014	n/a	The tax minister used his local business to transfer bribe money to diverse shell firms, ultimately to Liechtenstein accounts Nr. 42018000000000500
2014-2015	n/a	Deputy prosecutor general made payments for tuition and rent for his daughter at a UK university and to acquire real estate in Croatia using Seychelles, Panama and UK shell firms. Nr. 52016000000000495

(Table 21 continued)

2006-2014	n/a	Chairman of regional assembly failed to declare overseas wealth, including a luxury yacht owned by an SLP, used other shell firms with to buy real estate in Croatia. Nr. 42015040000000386
2014	$3.4mn	Odesa regional officials gave road-building contracts to allied local companies at a markup, with the funds being transferred from Ukraine to Cyprus and Panama shell firms, and then some to Swiss company accounts at Swiss banks. Nr. 52016000000000123
2015	n/a	Former top judge moved 13mn Swiss Francs from a Panama firm to a Liechtenstein bank not declared in his wealth declaration. Nr. 42015000000001756
n/a		A Swiss firm with Latvian account controlled by an oligarch made payments to BVI firm with Swiss account owned by brother of tax service head, as payment for return of VAT. Nr. 52017000000000700

4) Stolen funds are returned to Ukraine from foreign accounts via Riga-banked shell firms and paid out as cash or used to make acquisitions of companies or real estate (6 cases).

2011	$3.1mn	A publishing house paid $3.1mn to then president of Ukraine for authoring a book, funds came from a BVI shell firm. Nr. 42015000000001600
2012-2014	$32mn	State Agency for Investment and National Projects officials lent $32mn to two Ukrainian firms for drinking water improvement and for a Winter Olympics bid, the money went to Cyprus firms, UK and Panama shell firms, some paid into share equity of two Ukrainian firms. Nr. 42016000000001200
2013-2015	>$10mn	Former interior minister moved bribe money out of Ukraine to shell firms under fictitious contracts, from there transferred to Dutch entities he controlled, used to acquire real estate in Ukraine. Nr. 4201400000000100
2014	$20mn	State bank officials gave $20mn loan to a private agricultural company for kickbacks. The company transferred the loan to one Swiss and two Belize firms using fictitious contracts, $7.7mn returned to Ukraine ostensibly as share capital contribution. Nr. 32015000000000248
2010-2012	$400mn	State energy company officials purchased drilling rig from a UK shell firm for $400mn compared to manufacturer's price of $160mn, embezzling the remainder to accounts in Switzerland, while some funds repatriated to Ukraine and paid out as black cash. Nr. 42014000000000000
2015-2016	$5mn	State ports administration officials inflated the value of dredging contracts worth $13mn, the contractor paid the mark-up to UK and Cyprus shell firms, around $674,000 returned to Ukraine and paid out in cash. Nr. 52018000000000373

Source: USRCD

7.5 Case study of a bank

In this section I focus on the centrality of Latvia as an OFC, by examining the practices of the largest offshore bank, ABLV. As argued previously, Latvia is where global transaction banking integrated the post-Soviet shadow economy. Clearly the banks were at the heart of the assemblage performing this work ofintegration, but other informal para-bank structures such as ‘business introducer’ organisations, as well as the formal framework of Latvian state regulation and the informal practices of Latvian officials and parties, also played a role.

Latvia’s third largest bank and largest offshore bank, ABLV, was founded in 1993 and originally named Aizkraukles Banka until rebranding in 2011. It was owned by two Latvians and grew to become the largest offshore bank after the nationalization of Parex, Latvia’s third largest bank by assets behind two Scandinavian-owned banks (Aslund 2017). In February 2018, FinCEN issued a notice under Article 311 of the Patriotic Act designating the ABLV an “entity of prime money laundering concern”, which led to the bank initiating its self-liquidation after a withdrawal of licence (FinCEN 2018a, FinCEN 2018b). As a result of the FinCEN designation process, ABLV submitted a number of documents in its defence that were placed on file by FinCEN (ABLV Group 2015, ABLV Group 2016). In the next chapter I will examine the politics of the Article 311 notice; here I examine the documents provided by both FinCEN and ABLV to assess the bank’s activities.

FinCEN in their notice against ABLV in 2018 defined the service provided by the Riga offshore sector as reducing the risk ranking of financial transactions and thereby facilitating the circulation of CIS funds globally, which confirms my whitelisting argument.

> CIS-based actors often transfer their capital via Latvia, frequently through complex and interconnected legal structures, to various banking locales *in order to reduce scrutiny of transactions and lower the transactions’ risk rating* (FinCEN 2018b, my italics)

Analysis of ABLV shows that significant AML operations went together with significant ML operations, i.e. that the bank installed but did not apply AML technologies. ABLV could on paper claim to have implement sophisticated and expensive AML systems, according to the bank’s own AML audit. An interviewee close to ABLV defended the bank with reference to its expenditure on AML [interview #19 former Latvian finance minister]. Others with a neutral position said that the AML was a sham designed to satisfy correspondent banks, i.e.

part of the whitelisting strategy [interview #24 former Latvian banker]. According to the FinCEN allegations, the AML procedures masked money laundering operations that were directly supervised by bank owners and managers. FinCEN alleged that:

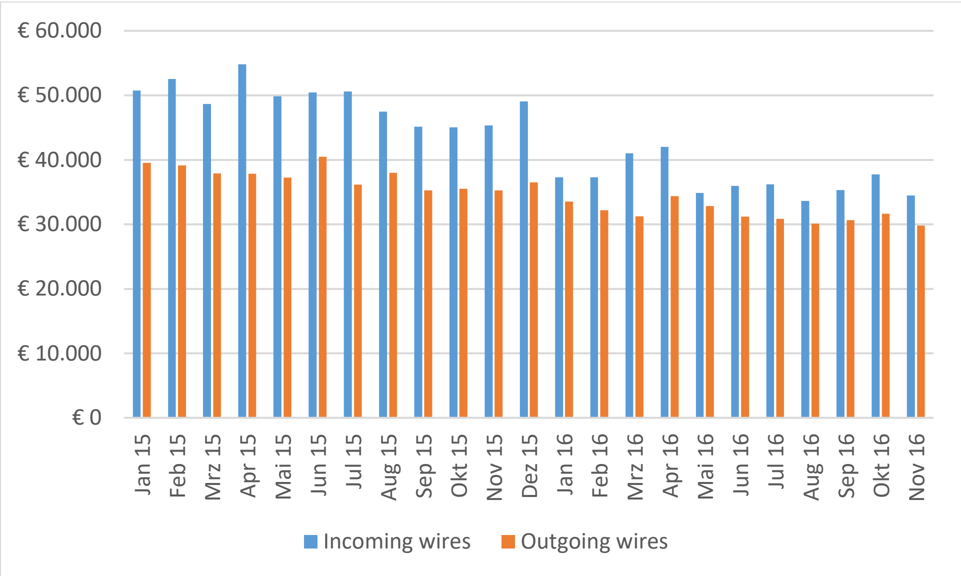
> ABLV executives, shareholders, and employees have institutionalized money laundering as a pillar of the bank's business practices (…) Management solicits the high-risk shell company activity that enables the bank and its customers to launder funds, maintains inadequate controls over high-risk shell company accounts, and is complicit in the circumvention of AML/CFT controls at the bank (…) In addition, ABLV management seeks to obstruct enforcement of Latvian AML/CFT rules (FinCEN 2018b).

Finally, according to the FinCEN analysis, the bank paid bribes to regulators. This indicates that part of the Latvian offshore sector's competitive advantages was that it enjoyed informal political protection on state level for its operations.

Examining the documents ABLV itself provided in its own defence shows traces of the business model I refer to as the integration of the post-Soviet shadow economy with US correspondent banking. ABLV had almost 13,000 shell firm clients in 2016, according to the bank's AML audits for 2015 and 2016. There is no breakdown by domicile of clients of ABLV but given the size of the bank it is likely that the overall breakdown of bank clients by jurisdiction for Latvia discussed in Chapter 6 applies to ABLV. As discussed, shell firms with hidden ownership act as a vehicle used to move funds out of the CIS countries, the authorities of which cannot identify the owners. This allows numerous schemes linked to trade-based money laundering - for instance falsified sale contracts - used to move money illegally out of the CIS states for tax evasion purposes or to launder illegal revenues (interview #25 Latvian anti-corruption NGO investigators). ABLV's AML audits show that UK clients were excluded from the high-risk client category requiring extra scrutiny (ABLV Group 2015, 2016). The bank only categorised as high-risk those transactions directly involving either CIS countries and / or secrecy jurisdictions, which totalled only roughly one third of incoming and outgoing payments (ABLV Group 2015, 2016).

The main business of the bank was transaction business, according to the bank's own internal AML audits. Customer deposits 2015-2016 were only \$3-3.5bn. However, in 2015, total client transactions incoming and outgoing totalled €54bn, more than twice Latvia's GDP, of which €28bn were incoming and €26bn outgoing, with payments in 2016 slightly lower. (ABLV Group 2015, 2016). This money was moved in hundreds of thousands of wires (funds transfers) coming and going from client accounts. There were 593,000 incoming wires and 730,000 outgoing wires to and from the banks' clients in 2016. Figure 19 shows the size of the average wire, month for month for 2015 and 2016, as calculated from the figures provided by ABLV. The relatively stable average wire size per month over the two respective years as shown in figure 18 may point to wires sizes being normed around a certain threshold value. Thus, these apparent regularities within the payment structure may arise from the widespread practice of 'smurfing' large amounts of money -i.e. fragmenting it into a number of smaller wires each below a certain threshold value - in order to reduce the risk profile. This again points to the active role of the bank in directing the ML business.

Figure 22. Average value of an incoming and outgoing wire at ABLV 2015-2016



Source: (ABLV Group 2015, 2016)

The money laundering activity alleged by FinCEN included the provision by bank employees of falsified documentation accompanying wire transfers, which corresponds to the '*konformashka'* described for the 1990s BoNY case described in Chapter 5:

> The bank proactively pushes money laundering and regulatory circumvention schemes to its client base and ensures that fraudulent documentation produced to support financial schemes, some of which is produced by bank employees themselves, is of the highest quality. (FinCEN 2018b)

These shadow economy transactions were largely but not exclusively linked to the CIS shadow economy, according to the FinCEN analysis. Major examples listed by FinCEN were:

> Moving a substantial amount of funds from a Russia-based bank in a manner consistent with an illicit transfer of asset;
>
> Funnelling billions of dollars through ABLV shell company accounts on behalf of Ukrainian billionaire on his country's most-wanted list for alleged embezzlement and appropriation of property;
>
> Large-scale corruption and money laundering by a politically exposed Azerbaijani using a shell company account at ABLV

These examples support my argument that the business model of Latvia's OFC was integrating the CIS shadow economy into the US correspondent banking network.

7.6 Conclusion

In this chapter I have examined the activities of Riga offshore banks in the shadow economies of the CIS states, from a threefold perspective: that of the customer jurisdictions, that of the target CIS markets, and that of the banks themselves. In doing so I have attempted to address a research deficit identified in Chapter 4 and thereby to 'bring money laundering back in' to the study of anti-money laundering. To do this I followed the ESRC research injunction to "explore the potential of new forms of data," and collated datasets from the surface web, deep web and dark web. The results of this chapter allow Riga to qualify as a shadow-economy OFC, pursuing a "Seychelles strategy" with a FATF-compliant veneer.

As discussed in Chapter 2, scholars generally define OFCs as spaces of exemption from regulations applying to individuals or companies in their domestic context. At the same time, scholars have called for analysis of new types of OFCs emerging under this umbrella definition, drawing attention to the increasing specialisation of OFCs (Sassen 2012, Hall 2018). Palan et al (2013) have drawn up a typology of seven current types of OFCs, as shown in Chapter 1, Table 1. However, the list does not include what scholars have called the "Seychelles strategy," where an OFC specialises in attracting criminal money, by providing non-residents with explicit exemption from AML, as the Seychelles did for some years starting 1995 (Unger and Rawlings 2008). Seychelles not only officially created a space of exemption from worldwide tax, but also officially provided exemption from criminal prosecution and assets confiscation worldwide. The “Seychelles strategy” is thus a “policy of deliberately inviting criminal investment,” becoming an OFC specialised in money laundering (Gnutzmann et al 2009 p245, Unger and Rawlings 2008).

As I have argued in this and previous chapters, Latvia like Seychelles competed on the global market for dirty money, and the CIS in particular. But in contrast to the Seychelles, which found itself quickly blacklisted, Latvia was able to do so for nearly thirty years because it combined formal regulatory ‘onshoreness’ with an informal practice of providing AML regulatory exemption to non-residents. In contrast to other OFCs, Latvia had no formal regulatory hallmarks of an OFC such as exemptions for non-residents from constraints in their place of domicile. Instead it had a highly deregulated but whitelisted financial sector, and an informal practice of exemption of non-residents from AML.

Encapsulating the parallels between Latvia and the “Seychelles strategy”, Seychelles shell firms in fact played a small direct role in the Riga offshore assemblage, while Seychelles shell firms disguised in a Scottish wrapper - as partners of SLPs - latterly became a hallmark of Riga banking, as described. Thus Latvia’s OFC can be seen as the “Seychelles strategy” wrapped in FATF-compliant clothes. The Latvian case thus qualifies the argument that “criminals need only to find the weakest link in the international financial system to have their funds cleared” (Gnutzmann et al 2009 p251). Recalling the definition of money laundering cited in Chapter 6 as the “false justification” of the legitimacy of money, laundering money requires also the addition of legitimacy to dirty money. This means an overt money laundering centre such as the Seychelles attempted to become is unlikely to succeed, because its funds will lack legitimacy. The Latvian case shows that for a country to export money laundering services, there should be a disparity between FATF-compliant status and the reality of financial services provided. Money launderers play on the arbitrage between FATF status and real / informal practices. In the next chapter I review Latvia’s discuss the circumstances under which Latvia was forced to end the offshore assemblage, examine Latvia’s informal ringfencing of AML, and explore what might come after.

Chapter 8. Closure and aftermath of offshore banking in Latvia

8.1 Introduction

While AML has been successfully adopted worldwide, evidence suggests that it is less successful in actually combating money laundering, as discussed in Chapter 3. Examining the Latvian offshore sector provides a partial explanation for this, given that money laundering is a performative practice that references the AML regime itself. As shown in Chapter 6, Latvia was whitelisted as a banking jurisdiction, while in Chapter 7 we have seen that the offshore banking sector in Riga was a hub for money laundering. I have argued that because the FATF regime was built on the power of reputation, legitimacy and normalisation, i.e. 'naming and shaming', which was the engine of its rapid expansion, it is in fact ill-equipped to deal with money laundering, at the heart of which is the feigning of reputation and legitimacy. The reification of risk manifested in AML's listing practices leaves it vulnerable to being gamed by launderers. In the previous chapter I illustrated how Latvia's offshore sector flourished both despite, and because, of the global AML regime.

Nevertheless, in 2018 Riga's offshore sector closed because of regulatory actions taken by the US. In this chapter, I show how state regulators in Russia, Ukraine and Latvia both colluded with, and contested Riga offshore banking, but only the US had sufficient autonomy to close it. The first section of the chapter deals with different states' regulatory actions in connection with offshore banking in Riga from 1998-2018, which are analysed from three different perspectives: firstly, that of the two largest client countries, Russia and Ukraine; secondly, from that of Latvia itself, and; thirdly, that of the USA, the regulator of the currency of offshore banking. I use Foucault's categories to discuss the intervention of the US in 2018 as being an act of sovereignty rather than governmentality.

In the second section, I draw on Nesvetailova and Palan's concept of regulatory 'sabotage' as a force of innovation in the financial sector to discuss how Riga banks sabotaged AML. I link banks' sabotage of AML rules and regulatory connivance to the informal ringfencing from AML of non-resident banking in Latvia. In the third and final section of the chapter, I draw on an analysis of online chat groups of offshore professionals to discuss what happened to the Riga offshore banking assemblage after closure in 2018, tracing the disbanding of the network and its incipient re-formation.

8.2 Contesting Riga. State-led regulatory action against Latvian offshore banking 1998-2018

In this section I initially examine attempts by regulators in Russia and Ukraine, the two largest CIS markets for Latvian offshore banking, to control and restrict the activities of Latvian banks from 1998-2018, before looking at regulatory actions taken by Bank of Latvia and by the USA. Both Russian and Ukrainian regulators showed at times that they were aware of the scale of the problem. However, given the extent to which Riga was embedded in the shadow economy in these countries, as discussed in Chapter 7, there was a lack of broad political will to deal with the problem, beyond the initiatives of some brave officials. In both Russia and Ukraine, the final strategy chosen was to extricate the banking sector from the shadow economy by closing banks implicated in dubious transactions, in both countries amounting to over half of the banks.

As described in Chapter 6, at the turn of the century after the debacle of the ruble crisis and Bank of New York scandal, Russia was blacklisted by FATF, while Latvia moved swiftly to adopt AML institutions. However, in a parallel process, starting in 1998, the Central Bank of Russia (CBR) itself blacklisted Latvia in 1998-99, in connection with the activities of Latvian banks in the 1990s as described in Chapter 5. In May 1998, shortly before the ruble collapse, the CBR required that banks set aside 100% reserves on all transactions with residents of Latvia, effectively closing interbank relations between Latvia and Russia. In 1999, Russia added Latvia to its 'black' list of jurisdictions considered offshore tax havens (Biznes & Baltiya 2003, Bank of Russia 2002). These restrictions on Russian banks' dealings with Latvia remained in place until April 2003. Russia later withdrew these restrictions in the process of its own moves towards joining Moneyval and FATF. The process of removing these restrictions lasted until April 2003 and was supervised by first deputy head of the Bank of Russia, Andrei Kozlov (Kommersant 2003).

In Russia itself, Kozlov headed Russia's campaign against regulatory infringements by banks, closing a number of offending banks and in so doing prompting a minor banking crisis. After 2003, Latvian banks were allowed to open representative offices in Russia again. But difficulties with Latvian banks quickly re-emerged after the removal of restrictions. In April 2006, Kozlov paid visits to the Baltics to discuss the practices of newly opened representative offices of Latvian banks in Russia, believed to be involved in money laundering, threatening a fresh clampdown (Vesti Segodnya 2006). In September that year, Kozlov was assassinated in Moscow, on the orders of the owner of a small money laundering Russian bank, the licence of which he had ordered to be withdrawn (Kommersant 2007). The banker was sentenced to life in prison in 2007 (Kommersant 2007). Several authors have linked the murder to Kozlov's attempts to clamp down on dollar outflows via Baltic and Central European banks (Bendtsen et al 2019, Daily Beast 2018, Moscow Times 2007).

After Kozlov's death, the CBR retained close supervision of interactions with Latvian banks. Possibly as a result, some major money laundering schemes involving Russian money and Latvian banks used other CIS countries as intermediaries between Russia and the Baltic states (interview #22, UK anti-corruption investigator). The notorious 'Magnitsky case' of 2006-8 involved hundreds of millions of dollars' worth of fraudulent tax refunds moved out of Russia by a group of small banks on behalf of corrupt tax officials and police, leading to the death in custody of whistle-blower Sergei Magnitsky (Browder 2015). In this case, dirty money from Russia only reached via Latvian banks after moving through banks in Ukraine, Moldova and Belarus (Reuters 2012, interview #22 UK anti-corruption financial investigator, Browder 2015). Similarly, the money-laundering scheme known as the 'Russian laundromat' saw around $20bn moved out of Russia via Moldova to Latvia by money launderers on behalf of their clients 2010-2014 (OCCRP 2014b). In a similar scheme, another $25bn was moved out of Russia via Belarus and Kazakhstan, before being moved to banks in the Baltics and Cyprus, according to the central banks of Russia and Belarus (Intellinews 2013).

In addition to using intermediary countries between Russia and Latvia, large flows of Russian money started to move via individual banks with close operating ties to Latvia, but operating out of Estonia, as discussed above, as well as Lithuania and Kyrgyzstan, despite repeated protests by the CBR (Bentsen et al 2019, Global Witness 2013). The CBR appeared to have been aware of the extent of illegal outflows out of Russia. In his 2012 retirement speech, long-serving CBR head, Sergei Ignatiev, referred to suspicious transactions in 2011 totalling $49bn moved illicitly out of the country by one matrix of shell firms, causing around $20bn losses to the state budget (Vedomosti 2013). "With a serious concentration of efforts by law enforcement agencies, I think it is possible to find these people," Ignatiev said pointedly (Vedomosti 2013). One of the small Russian banks involved included Russian President Vladimir Putin's cousin on its supervisory board. Thus, due to political protection and corrupt connections with the local money launderers, Russia's law enforcement took action only hesitantly against local money launderers while, in the Magnitsky case, were complicit in a cover-up (Browder 2015).

In 2013, under Ignatiev's successor, Elvira Nabiullina, the CBR launched a purge of the domestic banking system. This comprised the first concerted effort to change the sprawling commercial banking sector that was a legacy of the years of the Soviet collapse and its aftermath, as described in Chapter 5. This can be seen as an attempt to extricate the banking sector from its shadow economy activities. Between 2013 and 2018, the CBR closed over half of Russia's banks, at a rate of roughly three per week, reducing the total number from over 1000 to 414, with the final aim of having only around 300 banks (Kaurova 2017, Intellinews 2020). The grounds for over 40% of licence withdrawals were related to money laundering, with prudential violations comprising the rest (Intellinews 2020). "Positively, as a result of the clean-up the CBR has managed to effectively stop capital outflows via doubtful transactions," ratings agency Fitch concluded in 2019 (Reuters 2019b). However, it is too early to assess the real effect of the purge (Kaurova 2017).

As noted in Chapter 5, , US transaction banking meshed with the shadow economy in Ukraine, as in Russia, in the 1990s, partly also using Latvian banks as an intermediary. In 2000, the deputy head of the National Bank of Ukraine (NBU) accused Latvian banks of facilitating the siphoning out of Ukraine of billions of undeclared dollars using fictitious import contracts (Biznes & Baltiya 2000). Similar cases of billions of dollars being illegally moved out of the country via the Baltic states continued (Kommersant Ukraine 2007). In contrast to Russia, Ukraine had increasingly good relations with Latvia, since Latvia strongly supported Ukraine's European aspirations. Perhaps consequently Ukraine never acted against Latvian banks until 2016, when the NBU warned Ukrainian banks against operations with three Latvian banks in a letter (OCCRP 2016c).

In 2014, after a strengthening of Western oversight in Ukraine and a reform programme sponsored by the International Monetary Fund, a new NBU head launched a purge of Ukraine's banking sector similar to the Russian clean-up (Gontareva and Stepaniuk 2020). This led to the number of Ukrainian banks falling from around 200 to 81 between 2014-2018.. However, the clean-up campaign aroused resentment among (ex-)bankers that led to the reformist head of the NBU to resign and flee the country, claiming threats to her life (Gontareva and Stepaniuk 2019, Guardian 2019b).

Regulatory actions by Bank of Latvia

Latvian regulators withdrew the licence of four banks between 2006 and 2018 in connection with regulatory offences. Examination of these and other cases of regulatory actions in this section suggests this comprised largely reputation management following international scandals or pressure, i.e. Latvian regulators took strong measures only belatedly after major international triggers forced it to do so. These interventions confirm the argument made in Chapter 6 regarding Latvian regulators' protection of the offshore banks, and the trumping of regulation by reputational concerns. These interventions became more frequent with larger - although still relatively minor - fines after 2016, as international pressure grew on Latvia over its bank sector.

In 2006, Latvia withdrew the licence of Ogres Komercbanka, a small offshore bank with Ukrainian shareholders, on the grounds of "absence of internal control structures." (FCMC 2006, Telegraf 2006). Ogres Komercbanka, the clients of which were predominantly offshore companies, held bank accounts for a US shell firm implicated in a 2004-2005 Ukrainian investigation into nuclear-capable cruise missiles smuggled to Iran and China in breach of international missile proliferation agreements that had alarmed the US (Telegraf 2006, Financial Times 2005, interview #30 former US law enforcement officer). The move was interpreted as a symbolic gesture intended to placate the US, after in 2005 the US had sanctioned two Latvian banks, as detailed below (Telegraf 2006). In 2011, Latvia closed Latvijas Kraijbanka, a retail bank owned by Lithuania's Snoras Bank, which in turn was owned by a Russian banker (FCMC 2011). The move was triggered by Lithuania withdrawing the licence of Snoras bank after it encountered liquidity problems and allegations of financial impropriety (FCMC 2011). Latvian authorities then withdrew the licence of Latvijas Krajbanka, belatedly discovering a balance sheet hole of around $100mn due to insider unsecured loans (interview #10 former Latvian financial market regulator).

Following Latvia's accession to the Eurozone in 2014, the European Central Bank (ECB) formally became the banking regulator but operated on the basis of information provided by the local regulator. In April 2016, at request of Bank of Latvia, the ECB withdrew the licence of Trasta Komercbanka, a Ukraine-linked offshore bank. The move followed a succession of money laundering scandals highlighted in international media, ranging from billions of dollars laundered in Ukraine 2010-2014 and culminating with the 'Russian laundromat' investigation of $20bn laundered out of Russia via Moldova, detailed in Chapter 7 (FCMC 2016, OCCRP 2016a). In 2016, Latvia's FCMC imposed a fine of just over €2m on Privatbank Latvia and demanded that the bank council be replaced, after extensive coverage in international media of the banks' involvement in laundering over a billion dollars stolen from a Moldovan state bank through fraudulent lending, as discussed in Chapter 7. (FCMC 2016, Hromadske 2019). In 2017, FCMC fined five banks for breaching international sanctions on North Korea, using materials provided by the FBI to justify the fines. The initiator of this action was the US (see next section).

In February 2018, Latvia requested that the ECB withdraw the licence of the largest offshore bank ABLV, after a FinCEN Article 311 notice caused rapid deposit outflow (see below for a discussion of Article 311). Latvia then allowed the bank to self-liquidate under supervision of its shareholders, who were also the former management of the bank, despite misgivings from the US and civil society. Critics decried this as a potential cover up that would see the destruction of evidence of money laundering (Transparency International Latvia 2018). Here as well we can see a protective attitude by authorities towards the banking sector. As discussed in Chapter 4, a professional bankruptcy administrator, who had lobbied in the US against the self-liquidation decision and in favour of external liquidation of the bank, was assassinated in an apparent professional killing in Riga in May 2018, with no arrests to date (Caruana Galizia 2019).

In parallel to these events, a new Latvian player - with strong historical ties to the FBI - impacted on the offshore banking sector in 2018. This was Latvia's anti-corruption bureau, known under its Latvian acronym KNAB. Founded in July 2002, with strong input from the FBI, the KNAB had become a respected independent investigative institution that had brought criminal charges against at least one of Latvia's three 'oligarchs' (Kuris 2012, Karrstrand and Jonsson 2012, FinCEN 2019). However, while KNAB has successfully focused on domestic corruption, it had hitherto played almost no role in anti-money laundering or policing the offshore sector, evidenced by the low number of SARs sent to KNAB by Latvia's FIU (FIU 2017). In early 2018, however, shortly after the US Article 311 measures against ABLV, KNAB brought charges against the long-serving head of the Bank of Latvia, Rimšēvičs, for allegedly demanding bribes from an offshore bank in exchange for permission to launder money, marking its first case involving the offshore banking sector (Guardian 2018a). The charges were based on allegations made by offshore banks themselves of Rimšēvičs' attempts to extract bribes, although as discussed FinCEN also made such allegations in the Article 311 Notice. The investigation is ongoing (interview #9 former adviser to Latvian prime minister).

Thus, even in the case of the closure of ABLV, after serious money laundering allegations by the US led to the end of the offshore sector in its previous form, regulators permitted the bank's politically influential shareholders to oversee the bank's liquidation, prompting allegations of a coverup. In contrast to subsidiaries of Scandinavian banks accused of money laundering in Estonia and Latvia - Danske Bank Estonia and Swedbank Latvia - there has been to date no independent AML audit published of a Latvian-owned offshore bank (Clifford Chance 2020, Bruun and Hjejle 2019). This underlines regulatory connivance in the activities of the offshore banking sector.

US sovereign intervention against Latvian banks

In this section, I argue that it was not the governmentality-based FATF regime as discussed in Chapter 3 that contested and finally closed the Latvian offshore sector in 2018, but the actions of the US sovereign. Judith Butler conceptualises Foucault's categories of sovereignty and governmentality as being not a chronological succession, but rather denoting alternating modes of power (Butler 2004). Butler argues that in the US 'War on Terror', sovereignty returns to power in the form of US extraterritorial measures such as the Guantanamo Bay prison (Butler 2004). I argue that US sovereign power, not the FATF governmentality regime as discussed in Chapter 3, contested and finally closed the Riga offshore sector, jealous of the integrity of US jurisdiction and currency from criminal abuse and protective of US territory against perceived threats from weapons of mass destruction.

The first engagement of US sovereign power with Riga offshore banking was aimed at stopping use of shell firms incorporated in the US for international money laundering, as discussed in Chapter 7. Such abuse of US shell firms was seen as an incursion on US sovereignty by criminals. Thus, in cracking down on use of US shell firms for money laundering, the US was enforcing its sovereignty rather than acting within the 'governmentality' paradigm of the international FATF regime. As director of US Treasury's FinCEN Jamal El Hindi declared in 2006 when discussing the campaign against US shell firms:

> FinCEN's main goal in administering the BSA [Bank Secrecy Act] is to increase transparency in the U.S. financial system. (…) That is why finding a way to address the misuse of legal entities in the context of the BSA has been and continues to be a priority for the U.S. Department of the Treasury and for FinCEN. (El Hindi 2006)

The weapon US Treasury chose to use against 'abuse of US legal entities' was Article 311 of the 2001 Patriot Act, an expression of US sovereign authority over dollar transactions. Article 311 targets individual banks rather than countries. The US Treasury calls it "a powerful and flexible regulatory tool to take actions to protect the U.S. financial system from specific threats" (US Treasury 2011). Informally it is known as "banking's death penalty" (interview #30 former US law enforcement officer). In its full form, Article 311 rules to exclude a specific bank from the US correspondent banking system. As we have seen, between the initial rule-making proposal and the final decision, the targeted bank can submit documentation and arguments in its defence, meaning the actual ruling comes significantly later. The rule-making proposal itself however causes a voluntary abandonment of the named institution by its counterparties, crippling it, which renders the final ruling of less importance (Heifetz and Sherwood 2014).

As discussed in the previous chapter, up to 2005, 25% of deposits in Latvian offshore banks were owned by firms incorporated in the US. Latvian bank clients were the major user of US shell firms for money laundering (FCMC 2005). In 2005, as part of the FinCEN campaign against abuse of US shell firms, FinCEN issued notices under Article 311 of the Patriotic Act regarding two small Latvian banks, VEF and Multibanka. FinCEN alleged that the clients of both banks extensively used US shell firms to launder dirty money from Russia into the financial system. In 2005 the two Latvian banks were only the fourth and fifth banks to which FinCEN had initiated the Article 311 measure, following banks in Northern Cyprus, Syria and Myanmar, all three of which counted as rogue states (US Department of Treasury 2005). Latvian banks closed thousands of accounts of US shell companies as a result of the FinCEN intervention, with the role of US shell firms as depositors in Latvia falling to only 2% by 2011, replaced by UK and New Zealand structures, as described above (Dienas Biznes 2007).

US actions regarding global correspondent banks

Following the global financial crisis starting 2007-2009, US Department of Justice started to impose vast settlement payments on international dollar clearing banks for abuses connected to breaches of US sanctions and money laundering regulations. These settlement payments included in 2014 fines of $9bn imposed on France's BNP Paribas for violations of US sanctions on Sudan and Iran, of $2.6bn imposed on Credit Suisse for aiding US tax evasion, and $1.9bn against HSBC for money laundering, and in 2010 $160mn against US Wachovia Bank for money laundering for Mexican drug cartels.

I argue that such huge settlements were arbitrary actions taken by the US sovereign to shock rather than measures taken within the regime of governmentality as discussed in Chapter 3. Their sheer size pushed global banks to 'derisk', defined as "the phenomenon of financial institutions terminating or restricting business relationships with clients or categories of clients to avoid, rather than manage, risk" (FATF 2014). Derisking expressed the fear of US sovereign power felt by major correspondent banks:

> As one respondent put it "We're supposed to have a risk-based approach, but what we have is a fear based approach". That uncertainty makes it impossible to give it a monetary value—and quantify the costs in terms that can be factored in and dealt with as part of their overall risk-reward ratio assessment. (World Bank 2015 p29).

> US regulators were conducting, you know, a very intimate investigation of every single bank … no bank was exempt from the kind of rectal examination … And so the result of that was we were on notice that we better understand where every single dollar in our bank that our bank touched came from, because if it had connections with money laundering or terrorism or corruption or anything else, then, you know, the regulator was going to come after us (interview #26, UK academic)

Given the importance of geographical markers in AML, as argued above, such risk reduction had a strongly geographical character, resulting in US correspondent banks withdrawing from entire countries. Derisking alarmed international financial institutes such as IMF, World Bank and FATF supportive of global governmentality. According to a World Bank survey, around 75% of banking jurisdictions worldwide had noted that the US banks had started to withdraw their provision of correspondent services (World Bank 2015). US correspondent banks became apprehensive about their responsibility to “know your customers’ customers,” referred to in the AML jargon as KYCC. This was particularly relevant for the transaction business with Eastern Europe (World Bank 2015). Thus, derisking directly impinged on the offshore banking sector in Latvia.

> The Baltics was an area where [bank] had a very active business. And, you know, when you started to look at it, you started wondering whether that activity was activity we should be supporting. (…) Can you genuinely know where this money's coming from? We didn't get a satisfactory answer. (interview #26, UK academic)

In 2007, one of the five major US correspondents for Latvian banks - Bank of America - withdrew from the Latvian market, as part of a derisking strategy (Dienas Biznes 2007). The remaining banks providing direct correspondent relations to Latvia were HSBC, JP Morgan and the US subsidiaries of German banks Commerzbank and Deutsche Bank. US investigation of HSBC for laundering of Mexican drug money resulted in a $1.92bn fine in 2012, prompting its withdrawal from many markets including Latvia (BBC 2017b). In January 2014, JP Morgan closed its correspondent accounts for Latvian banks, amid a worldwide purge of its correspondent accounts after US warning to boost AML controls (Bloomberg 2014b).

This left only two direct US correspondent accounts available to Latvian banks - both the US subsidiaries of German banks Deutsche Bank and Commerzbank (Bloomberg 2014b). In 2015, Commerzbank was prosecuted by the US Department of Justice and paid $1.45bn for dealings with Sudanese and Iranian entities, prompting its withdrawal from many markets, including Latvia (Department of Justice 2015). Thus by 2017, there was only one direct US correspondent banking relationship available to Latvian banks, with Deutsche Bank Trust Company Americas, the US subsidiary of Deutsche Bank. Offshore banks however frequently used nested correspondent banking relations, i.e. access US clearing via a European, often Austrian, intermediary, but this raised costs for transactions as much as tenfold (interviews #29 British AML officer, Dienas 2007).

At the start of 2017, Deutsche Bank then closed its Latvian correspondent accounts. It did so as part of worldwide withdrawal following on the Danske Bank Estonia scandal mentioned in Chapter 7, which saw Deutsche Bank reduce its total correspondent accounts by 40%, and high risk accounts by 60% 2016-2019 (FCMC 2017, BNN 2017, Reuters 2019). This left Latvia's offshore bank sector without direct dollar clearing for the first time since independence. The withdrawal of direct dollar clearing was accompanied by a sharp reduction in dollar transfers, and sparked protests from pro-bank voices.

> Latvia, a highly-respected member of the European Union, is left with minimal correspondent banking relations. Neither the ECB nor the IMF can sort out this problem because it stems from the relationships and understandings between the large banks with operations in the US and the Federal and state bank regulators (Aslund 2017).

As argued, the loss of correspondent accounts was not related directly to Latvian bank activities, but reflected correspondent bank derisking driven by fear of the US sovereign. Latvia tried again to improve its banks' reputation, such as conducting an AML audit of banks, organised by FCMC in 2016, and also belatedly tightened the reality of AML compliance for banks starting 2016 (interviews #10 former Latvian financial market regulator, #18 former Latvian finance minister).

US actions regarding North Korea sanctions

With the inauguration in January 2017 of Donald Trump as US president, the US administration switched from a 'governmentality' mode of foreign policy using a dense network of allies and institutions, to the 'sovereignty' mode, also termed a transactional foreign policy (Hadar 2017). Henceforth the US would use its sovereign power in an arbitrary fashion to obtain results in its immediate interest (CNN 2019). Rather than enforcing international rules, this involved punishing declared enemies of the US, and in particular North Korea and Iran. It also involved making sure recipients of US security guarantees, such as Latvia and Germany, fully complied with US interests (Council on Foreign Relations 2019).

In 2017, this new approach led to a rapid escalation of tension between US and North Korea, including an escalation of sanctions and tightening of monitoring of existing international sanctions against North Korea. As a result of this, five Latvian banks were fined by FCMC for breach of North Korea sanctions, on the basis of material provided by the FBI (FCMC

2017b, FCMC 2017c), as noticed above. According to the UN Security Council ‘Panel of Experts’ on North Korea sanctions:

> From 2009 to 2016, banks in a European Member State were used by foreign organized crime syndicates to circumvent the sanctions regime, including for the export of goods and equipment related to the prohibited programmes of the Democratic People’s Republic of Korea. Customers at several banks transferred funds in a series of complicated transactions involving accounts held by offshore companies for the benefit of entities of the Democratic People’s Republic of Korea. (UN Security Council 2018 p171)

The respective banks gave signed declarations that they would not relapse. However, in February 2018, FinCEN issued a notice of proposed rule-making under Article 311 regarding ABLV, the largest offshore bank, and Latvia’s third largest bank (FinCEN 2018a). ABLV’s alleged offence was to have conducted further North-Korea related transactions after the 2018 warning (FinCEN 2018b). The notice prompted an immediate run on deposits at the bank, triggering the ECB to withdraw its licence. Latvian regulators then controversially allowed the bank to self-liquidate, as discussed above.

As a result of the ABLV case, as a demonstration of loyalty to US, and under US supervision, Latvia moved to close the offshore banking business. The US Treasury directly monitored the winding up of the offshore sector in Latvia. The Assistant Secretary to the Treasury, Marshal Billingslea, who also *ex officio* assumed the rotating presidency of FATF from 1 July 2018 for one year, personally visited three times in Riga in 2018 and 2019 (LSM 2019). Billingslea made clear in a May 2019 interview to Latvian media that it was the wish of the US that the offshore sector be closed:

> The U.S. and Latvia are close NATO allies. We stand with the government as it is moving to clean up a very difficult situation that has been accreted over several decades - poor policies, lax oversight and weak enforcement. In fact the government is coping with a banking sector that was specifically designed to attract non-resident deposits and offshore accounts, and that has led to the situation Latvia finds itself in, which is that it has a banking sector that remains one of the most vulnerable in Europe. It has a banking sector that has a history of exploitation by organized crime, by foreign governments that are hostile to NATO and [have] outright corruption in society (LSM 2019).

Billingslea's comments here also mark a shift in emphasis from the North Korea allegations to Riga banks' overall association with Russia, as the Trump administration sought to distance itself from Russia because of allegations of Russian contribution to Trump's election victory in 2016.

Thus within three months of the FinCEN decision, Latvia's parliament amended the AML Law on 9 May 2018, to ban bank accounts for shell firms, defined by a "lack of documented proof of real business activity and lack of submission of annual financial statements" (FCMC 2018). The amendment caused the closure of 9000 shell firm accounts within a sixty-day period (FCMC 2018). By August 2019, 17,000 accounts had been closed (FCMC 2019). Latvia conceded to US requests to limit non-resident deposits to 5% of total deposits of the Latvian banking sector (interview #27 Latvian broadcast journalist). Apart from the legislative changes, the US also supported a reboot of Latvia's FIU and FCMC under new leadership (interviews #27 Latvian broadcast journalist).

As a result of these measures, the volume of foreign deposits in Latvia's bank system declined by 74% 2015-2019 (from €12.4bn to €3.2bn). Domestic deposits in 2019 accounted for 80% of total, compared to 45% in 2015. Non-euro transactions fell from $269bn in 2015 to $40bn in 2019 (FCMC 2019). Latvia's government symbolically removed reference to developing Riga as a financial centre from its development plan (interview #27 Latvian broadcast journalist). Knowing that the end had come to offshore banking in Latvia, some banks froze large amounts of depositors' money, ruling it of suspicious origins, which accelerated the winding up of the sector. Respondents agreed that although there were attempts to find a business model oriented towards the local market, the banks that comprised the offshore sector had no future, and following the US intervention the sector was effectively "a corpse" (interview #19 former Latvian finance minister).

8.3 Reviewing Riga. AML 'sabotage' as informal ringfencing of Latvian offshore banking

In this section I use the term 'sabotage' as it is derived from the institutional sociology of Thorstein Veblen and applied to contemporary finance by Nesvetailova and Palan (Nesvetailova and Palan 2020). Nesvetailova and Palan define sabotage as:

> the constant fight against competition and for market control [which] means that our financial intermediaries (…) bypass existing regulations, grow in power and autonomy, undermine competitors and exploit customers and the public resource (Nesvetailova and Palan 2020 p170).

Nesvetailova and Palan see banks' desire to sabotage - both evade and exploit - regulations as one of the stimulants of financial innovation, arguing that "[t]hroughout history, financial innovation has always had a regulation-evading intent built into its techniques." (Nesvetailova 2018, p240). At the same time, financial innovation exploits regulations to create new profit-making opportunities. As I have argued above, Riga banks not only evaded the AML regime but also exploited its algorithm of cleanness, thereby "exploiting regulatory niches and carving out new ones" (Nesvetailova and Palan 2020 p170). Thus Latvia's offshore banking sector enjoyed informal ringfencing with regard to AML regulations, which I argue was a defining feature of Latvia as an offshore financial centre. 'Sabotage' of AML meant that Latvian offshore banks competed on the global market of money laundering services, thus pursuing the 'Seychelles strategy' while remaining formally FATF-compliant.

The consensus among respondents was that Riga banks were able to override the AML system as it had been created in Latvia. A former official at FCMC described the problem as follows:

> … the legislation was class-A legislation. As you can see from our Moneyval report, our legal framework is and also used to be one of the best, one of the tightest ones, but there are questions about its effectiveness … Initially like in any jurisdiction we thought it is just a question of having good laws in place. It definitely turned out that's probably not enough. [interview #18, former FCMC official]

As is suggested here, there was lack of effective enforcement of AML laws in Latvia. While there was a consensus view that this was the case, there was more disparity of opinion about the reasons, be they of oversight or intent. A former finance minister believed that the reason for the underfunding of AML institutions was simply "the lack of understanding of the risks," and that there was no specific intention behind this:

> That was not done intentionally it was just that the whole concept of financial crime, the institutions were unfamiliar with the danger of it and probably only went when we could see or observe that Russian money is influencing the election results both in the

> US and the European Union that I could understand that it was really a question of not only the economic stable stability but it is a question of security as well. [interview #14, former finance minister]

The second group of respondents however believed strongly that regulators and politicians had been complicit in rendering the AML ineffective for political and corruption reasons, i.e. there had been capture of the regulator by the offshore banking sector, ranging from capture of legislation to the bribing of leading financial regulators. An investigative journalist said that the banks wielded influence over all banking legislation, leaving the regulators' hands tied by the specific provisions of laws.

> [T]he banks were very, very powerful and it was they who created all that legislation about banking system. [FCMC official] was a very good lawyer with a very clear vision of legislation ... And he said the legislation is created by banks. So that's why he was always on the banks' side. [interview #16, Latvian investigative journalist]

The former adviser to the PM suggested that ultimately Latvia's oligarchic political structure was to blame for the failure of AML institutions and regulators to operate effectively:

> Our political system (…)was infected (*sic*) by at least three oligarchs who have been dominating politics for the past 20 years or so. I think it was in their best interest that the justice system was very ineffective and the law enforcement agency they were very ineffective in dealing with all sorts of financial crime. [interview #9, former aide to Prime Minister]

None of the 'oligarchs' referred to were bank owners, but they had made their money in the transit trade linked to Russian commodities mentioned in Chapter 5, which was a source of funds for banks, and due to their political influence, they could provide protection to the banks.

Other respondents focused on alleged shadowy networks between financial sector regulators, politicians and banks dating back to the 1990s. This refers specifically to the case of the long serving head of the Bank of Latvia, Ilmārs Rimšēvičs, who had been deputy head of the Bank of Latvia in the 1990s, before heading the Bank of Latvia 2001-2018. According to another former finance minister, the financial market regulator FCMC continued to be Rimšēvičs' "fiefdom" despite being formally independent of the Bank of Latvia. According to the former minister, the Bank of Latvia official in turn was supported by the banks, via an anti-corruption political party “New Era”.

> at the beginning of this century, Repše set out to create a political party and he would go after corruption and it would be cleanest of clean and so on, and for that I need $1mn [he said], so that I would not have any “proclivities” to anything, and this one million, it was assembled, believe it or not, and guess where it came from, most of it: The banks. The interesting thing is that talk in the industry says the banks killed two rabbits with one shot: they got Rimšēvičs as head of the Bank of Latvia, and at the same time the new party ‘New Era’ provided political support for him, ensuring he was reelected as head of the Bank of Latvia time after time, without any questions. [interview #19, former finance minister]

The former finance minister explained the crisis in the offshore banking sector post-2015 as the result of a breakdown in secret understandings between the Bank of Latvia and the banks. While some of this commentary may have partisan political motivation, some bankers also expressed little surprise about the charges brought against Rimšēvičs:

> And therefore, its ok for my bank to be clean but Latvia Inc needed to come on board as well, and a lot of guys didn't. And a lot of guys got away with it. (…) the governor of the Central Bank [Bank of Latvia] was accused of facilitating a lot of this malpractice, there is a court case pending. And I knew the guy personally very well and let's say it was a battle trying to get things done. [interview #23, former Latvian bank manager]

One respondent - a shareholder in a Latvian bank - alleged that an intermediary for top bank of Latvia officials collected bribes in exchange for banks being allowed to launder money.

> [the intermediary] said that all banks paid bribes in return for laundering money and I would have to play by the same rules (...) All Latvian banks “cooperated” in this manner, which was why none of them had faced difficulties with anti-money laundering regulations. ... The intermediary also proposed that he knew of a number of small Russian banks that wanted to ‘transit’ money out of the country. I believe that this must have been a kind of proposal put forward to, and frequently accepted, by many Latvian banks in and around this time [interview #6, former Latvian bank owner]

There are significant arguments that the failure of AML institutions in Latvia was due to informal networks of complicity between regulators and money laundering banks, i.e. there existed an informal ringfencing of the offshore banking sector from AML rules.

In what sense did banks override AML? One bank manager recalled that the recurrent argument from Russian clients was that they needed to use shell firms not for tax evasion, but to protect against extortion by criminals wore thin, but was largely accepted by the banks. [interview #23, former Latvian bank manager]. According to a Council of Europe investigator, the high volume, low margin transaction business was not compatible with customer due diligence, meaning that banks effectively opened the doors to money launderers:

> They [the banks] do not know their customer. (…) it's very difficult for them to implement that in an efficient way. (…) They earn a very small turn fee on the money flows, right. But these money flows are gigantic. And for the launderers it is a fee they are happily willing to pay. (interview #11, former Council of Europe investigator)

Another respondent, an AML officer, argued that tax evasion schemes were central to the business model. The respondent recalled an interview with a top manager at a leading offshore bank:

> I said one of the things that challenges me is why these companies, all these UK LLP entities, with all the money flowing through (...) why do they not have a website? (…) He [top Latvian bank manager] said that's simple to explain: the Russian companies sell the goods, and the U.K. LLP invoices. (...) So hang on. The Russian company sells to the Russian consumer. And then the UK LLP takes the money. He said Yes. Well at any level is that not called tax evasion and therefore we are laundering the proceeds of crime? [respondent asked the manager] And the look on his face as you have just explained money laundering to him. (…) They think tax evasion is not a crime, they think tax evasion is fine (interview #8, former US bank AML officer)

Other respondents believed that the bankers earned directly from money laundering, taking a cut of laundered funds, rather than merely earning commissions on the transactions.

> The majority of Latvian banks were doing this [money laundering]. This was their main business (…). It was well-known actually how much it cost [the cut] people were

> telling us how it was structured (..). What we heard was that it was 3-4% for the total turnover going through an account, and if you were lazy enough to not produce any paperwork behind the transactions then the banks would happily assist you for another 0.5% (…) providing you with all sort of fake contracts, invoices and so forth. [(interview #22, UK anti-corruption investigator)

The respondent believed that the proliferation of redundant payments was the main method the banks used to launder money:

> This was the usual way of doing it, they drag it through several accounts and make it more difficult to them and sometimes they'd be bounced back between Baltic accounts back and forth (interview #22, UK anti-corruption investigator)

A former US law enforcement officer commented on the role played by account managers at Latvian offshore banks. They handled queries from US correspondent banks on suspicious transactions by clients, for instance in the case of a 'laundromat type' company with high frequency and wide geography of inflows and outflows. When asked about their understanding of such a shell firms' business, the account managers at the Latvian bank would reply to the correspondent bank that the beneficiary was known to the bank, the transactions fitted the shell firm's trading profile as explained to the bank, and thus there was no cause for alarm. In reality the beneficiary was a proxy (straw man), and the trading profile was simply a broad category such as construction or car parts specified to clients of the laundromat to draw up fake documentation for payments (*konformashka*) (interview #30 former US law enforcement officer). This pattern of interaction in itself encapsulated the performative money laundering practice of the banks.

The activities of Latvian banks thus correspond to what Nesvetailova and Palan hold to be sabotage of regulations. "The more regulations are imposed, the more business opportunities are there" (Nesvetailova and Palan, 2020 p116). Thus, the competitive advantage of Latvian offshore banks was their provision of money laundering services that have been prohibited worldwide, while as a jurisdiction remaining superficially compliant with FATF. In the case of Riga, regulators also connived in such sabotage, creating a situation of informal regulatory ringfencing of the offshore banking sector from AML. The bankers mandated to act as 'big brother' towards clients in fact acted as 'black sheep' i.e. defected from, or sabotaged the AML regime to receive higher profits. As discussed in Chapter 2, characteristic of the offshore world is the regulatory creation of a ‘space of exemption’ from onshore constraints. In the case of Latvia, this space of exemption was created informally through the sabotage of AML. Such informal ringfencing in turn ensured Latvia’s continued whitelisting as an onshore respected jurisdiction. For this reason we can call Latvia an ‘onshore OFC’.

8.4 Re-assembling the network: Where did all of Scotland go after Latvia?

An important debate in sociology of finance and critical geography deriving from actor-network and assemblage approaches relates to change. As discussed in Chapter 4, while sharing philosophical roots, assemblage theory derives more directly from the work of Deleuze, whereas Actor-Network Theory (ANT), while inspired by Deleuze, was conceived in Science and Technology Studies. Given that Actor-Network Theory describes an existing constellation, it is seen as focused on continuity, whereas assemblage theory deriving directly from Deleuze is more open to change as rupture:

> ANT is better attuned to fluidity, meaning change without rupture, whereas assemblage thinking shows a greater openness towards the aleatory and unpredictable, towards the event. (Muller and Schurr 2016 p226)

The abrupt ending of offshore banking in Latvia in 2018 thus raises the theoretical question of whether the actor-network or assemblage reconfigures in a new form, as ANT might anticipate, or whether it disappears under the impact of the event, as assemblage theory might postulate. On an empirical level, the question of continuity or rupture also raises the question of whether dirty money flows can be controlled by administrative means, as the AML regime assumes, or whether “water will always find its way” (Unger and Hertog 2012 p287). This is crucial for AML because if the AML system of controls and closures simply cause the ‘water’ to ‘flow’ by a different route, rather than damming it permanently, then the value of such an intrusive system is questionable.

This section explores how offshore practitioners - mostly from the ‘business introducer’ profession described above - reacted to the closure of the offshore sector in Latvia, as reflected in contributions to a professional chat forum, the parameters of which I described in Chapter 4. Their reactions oscillate between a reflection on the Riga offshore sector, and discussion about what could replace it, in particular how to match suitable legal vehicles (offshore firms) with suitable banks, as had been the case previously with the ‘prestigious’ shell firms and Latvian banks. The comments all followed the closure of ABLV in 2018 through 2020. I have redacted the names of most banks. An arrow (→)indicates a new contributor.

One thread of the chat groups is that Latvian offshore banks are finished, after the US effectively cut access to dollars transactions in 2018, and they are now concerned only with expropriating depositors.

> →It’s a Latvian bank, what dollars are you talking about?
>
> →Latvia is finished, you don’t land in the same crater twice
>
> →When Parex collapsed [in 2008], {Latvian] Banks X and Y phoned clients in Ukraine, Belarus, Russia and offered them to switch immediately to them by opening accounts using only copies (!!!) of documents. The main target were the clients. And now, clients are no longer needed. Only their deposits. Thus there is the corresponding behaviour [of seizing client deposits] - cynicism is all it is.

Participants in the chat group from time to time post a message intended to take stock of the discussion about the offshore banking industry in the wake of the events of 2018-20. Some of these usefully summarise the arguments that the ‘shadow economy’ offshore finance was closed down by the actions of US regulators in Europe and elsewhere in 2018.

> → Colleagues ;) While there is free time, allow me to summarize some of the results of our fruitful discussions:
>
> 1. The offshore industry in the form in which we knew it - is dying before our eyes. Introducing [a requirement for offshore companies to prove they have economic] substance on the [offshore] islands is a nail in the coffin for assets-holding offshores. ("Payment" offshores are obviously already dead).
>
> 2. There are no really operating banks on the planet (with the possible exception of the USA) that are absolutely tolerant to gray area finance, any kinds of loans [as justification for making payments], the purchase of “debts”, “goods deliveries” without shipping documentation and so on.

> 3. The degree of tolerance of banks varies in different countries (ahead of all EU), but the trend is obvious. The closure of Armenia, Montenegro, Serbia and others like them is a matter of time. They are the next in line after Cyprus and the Baltic States. Maybe Ukraine will step up, but so far nothing has been heard ...
>
> 4. Bitcoins and shitcoins are not an alternative means of payment in real big business, anything above the level of the Moscow Sadovod market [Moscow’s largest wholesale market]. Maybe something like this will be in the future, but for now this is not obvious.
>
> 5. The numerous payment systems [EMIs] are not equal to high street banks in terms of functionality. They solve problems for small businesses and individuals. XXX did not become a new Barclays. Large payment systems (for example, YYY Bank in the UK) receive banking licenses and become banks with all the ensuing consequences.
>
> 6. Finally, after 2014, any “Russian” business in the West is now under double or triple control. By "Russian" we mean Russian speakers from Russia, Ukraine and Belarus, as well as other CIS countries. Business is possible, and perhaps even is very successful, but try with “Russian money” to get into some kind of sensitive sphere in Europe - into regulated finance, into banking, into insurance - and you will be immediately put straight ...
>
> What conclusion can be drawn from all this? Very simple. We must accept the reality as it is and rearrange it. Pay taxes. For those who have not yet readjusted and still do not pay. Or go out of business and trade on the Sadovod market
>
> Plus, “fixers” [business introducers etc.] have no future. There is a future in the industry for professional lawyers, tax consultants, auditors, bankers, and compliance officers. All of whom are regulated.

There are two parts of this argument. One is that the US is conducting a campaign against grey financial flows in general

Examples of the first argument are:

→The offshore world has 'shrunk' under political pressure from the EU and USA. Changes in form and content taking place today won't change anything, any signs of schemes involving offshore zones will scare compliance services in any organisation. Schemes will henceforth be individual, there will be no universal solutions and such a [chat]forum [as this one;won't provide any answers.

The second argument is that it is first and foremost a campaign against Russian money abroad:

→It is idealistic to think that everything will be fine if the bank is in the same country as the legal registration [of the company], if the counterparties are also ideal: They are storming offshores not because someone hasn't paid taxes or has used them to hold real estate. Europe and USA are conducting a disinfection of shadow Russian capital after it started to influence politics.

→The topic of all possible sanctions and prohibitions is simply the result of pressure from a country known to us all on all states with 'Russia orientation'. The attack on the Baltics means that all attempts to open an account with a serious bank will encounter problems.

Conversely, even though the chat group comprises participants in Latvian offshore banking sector, some contributors are prepared to acknowledge that the US was right to crack down, arguing that Latvian banks were simply "→machines for making payments from BVI to Belize" and "→Latvia and honest import is an oxymoron."

→Banks earned not on tiny interest or on commissions, but on grey and black schemes. Latvian banks - the more they had been laundering, the more prejudiced [unfair] was their relationship to their clients after the recent events [in 2018], in order to distract suspicion from themselves and their basic schemes.

→Problems in Latvia have occurred regularly since 1996. And nobody learnt anything. The minus is that such regions / banks started to spread out in the world - basically - an industry for siphoning money

→I read your messages and I just can't stop laughing. Well, we are all grown-up boys and girls. Let's stop pretending that "Princesses don't pooh" at least among ourselves.

> Let me put it like this: Baltic banks have always been engaged only in transit [of money] (…) for Russian-speaking business. This has been the case since 1990, when the free exchange of hard currency was introduced. The older generation still remembers how Parex Bank opened a branch in the Embassy (!!) of Latvia in Moscow at the beginning of the 90s and gave out 💰💰💰 in bags. And they lived beautifully on it.
>
> In any Moscow office of law firms of the type "offshore / accounts" lay packs of pre-opened Baltic accounts with numbers, where you only had to enter the name of the client. The bank client tokens (they had only just appeared) lay in bulk.
>
> When the rules changed and they jumped all over this business, the Baltic banks understood absolutely correctly that there was absolutely no place for "Russian" money, and it was their "New Oil" to milk the unresponsive suckers. Especially after 2014, when "Russian business" is not welcome anywhere, and it more and more resembles one big plague reservation ...

Many others view the crackdown as clearly discriminatory

> →There is professional disinformation. When a nit from a bank does not want to believe that he is stealing money from someone's family, it is convenient to justify it as "this is FSB blood money."
>
> →I understand that there are high risk customers who must bear additional costs if they wish to work in a bank. But what some Latvian banks are doing now in relation to clients from the Russian Federation, Ukraine and other CIS countries is barbaric and lawless.

A third argument alleging discriminatory action points to the supposed difference in strictness of regulations between the domestic US banking sector and standards applied by US bodies such as FinCEN internationally.

Rewiring the network?

One particular focus of discussion concerns the linkage between banking hubs and legal vehicles that they might ‘bond’ with, as was the case for Latvian banks and SLPs. This again highlights the links between banks, ABS (in this case the fixers / business introducers) and legal structures discussed in Chapter 1. Clients who owned SLPs and business introducers scrabbled to find new banks, as Latvian banks closed their accounts en masse in 2018. “Where did all of Scotland go after Latvia? Or did they bury all those firms?” asked one chat participant.

The answers:

> →In 2018 they ‘parked’ Scotland in Hungary, Czechia, Macedonia, Montenegro, Belarus, Austria, Liechtenstein, Luxembourg. They also went for payment systems en masse. Now things are even tougher but there are still options. But the general trend is no herd [movements] anymore but individual working solutions for each client and his requests. In brief: offshores of different degrees can now access only ‘strange’ countries / banks, such as Georgia, Kazakhstan, Belarus, Mauritius and other exotic ones.

Hopes were placed on other former socialist countries in the EU, in particular Czech Republic and Hungary. However, most agreed this involved setting up new companies for the purpose

> →Resident companies: you can create a Czech, Bulgarian, Polish, Estonian company, etc., but this is not a panacea. For example, you will not be able to open an account in the country or registration [locally] for an Estonian or a Czech company if there is a non-resident 'inside’ [as beneficiary]. It is also not the same as a Scotch [SLP], there is bookkeeping, etc. required (some forget this). But still many have moved from offshore / LPs to resident companies.

Chat participants noted that it had become impossible to acquire new SLPs, even posting rejection letters to this effect.

Another option discussed by chat participants are the classic European banking locations of Cyprus, Switzerland, Liechtenstein and Luxembourg. But Cyprus is regarded as having been closed down together with the Baltics due to its close links to Russia. Switzerland is regarded as an expensive and slow banking jurisdiction orientated towards savings accounts, with large minimum deposit requirements and expensive commissions for payments, with banks closing accounts that have frequent in and out payments.

Electronic Money Institutions

Chat participants highlight Electronic Money Institutions (EMIs) as one of the main new financial channels replacing Latvia and the Baltic banks. EMIs generally do not have bank licences, but facilitate payments in Euros via correspondent banks. The Baltic state of Lithuania has emerged as a pioneering jurisdiction for EMIs, having licensed over 150 fintech firms to date. Owners of SLPs and other clients of Latvian banks see payment systems as a real alternative to Riga, since the Riga-banking business as discussed was focused on making payments through the international financial system rather than the traditional banking business of loans and savings.

> →EMIs: there are lot of them and they are very varied: Some of them won't open an account for you [with SLP], others will without any problems. The clients are also very varied. But they are a real alternative to banks now, especially for making payments, not for savings. There are interesting variants. But still a lot of the old crowd believe that an account can only be with a bank.

In addition, chat participants believe some payment systems to be directly controlled by Latvian banks, meaning that some customers see in them a direct continuation of Riga banking.

> →Nothing changes. All the financial services are concentrated in the same "square" [of Riga town centre streets]: Elizabetes, Vesetas, Terbatas, etc. Now only the registration numbers [of EMIs] are from London .... so what was the point of their fight with shell firms then?

> →[bank] has chosen thus to use the money it expropriated from its customers [to build an epayments system]. In brief, the Baltic ecosystem is changing, we, the clients, need to change too.

Payments systems in particular are regarded as open to working with SLPs and traditional offshores, including with owners from former Soviet countries. Moreover, chat participants themselves consider opening and running EMI type services. Some participants looked to buy an operating EMI themselves, while others offered for sale or sought for purchase small working EMIs on behalf of clients. Thus, in terms of scale, EMI systems are smaller than an individual bank, and may use a Baltic bank as correspondent bank. Thus they do not replace the banks as much as the para-bank 'business introducer' organisations,

> →Operating a payment system is only partly useful, because all depends on the correspondent bank, and its price list, but it's difficult to find a correspondent for dollars, and prices are also not easy, as a result you get all the high risk like forex, gambling, chargeback, and you will quickly get closed down

Indicative of the money laundering risks connected with EMIs, Epayments, registered in the UK with a British licence, but with accounts at Rietumu Bank in Latvia, was one of the larger epayments systems catering in particular to former Soviet countries, until in February 2020, the Financial Conduct Authority (FCA) suspended its operations due to insufficient anti-money laundering controls (Leaske and Smith 2020). Investigative journalists have identified a number of other British registered EMIs run by former executives at Latvian banks, registered and licenced in UK, but with bank accounts at Latvian banks, and targeting business operations across the former Soviet countries, now providing euro transactions. "UK-regulated electronic money institutions, or EMIs, are being touted as a replacement for networks through which billions of dollars of dark money moved in and out of the former Soviet Union" (Leaske and Smith 2020). Therefore, returning to the opening enquiry as to continuity or rupture in the Latvian assemblage, we can see initial signs of the Riga network being rewired via the new technologies of EMIs, while retaining the 'whitelisting' strategy of UK registration. However, it is not yet clear that such system can again provide anything like the scale of financial flows previously seen via Riga.

8.5 Conclusion

I have argued that it was the US acting in a 'fit of sovereignty' that closed Latvian offshore banking in 2018, firstly because of allegations of breach of North Korea sanctions, but also because of tension with Russia over alleged election interference. In its action, the US was acting based on sovereign interests outside of the governmentality of the FATF regime discussed in Chapter 3. Latvian regulators acting in the framework of the FATF AML regulations only took measures when external scandals and pressure prompted them to do so, i.e. for reputational reasons. Russia and Ukraine, the two largest markets for Riga offshore banking, acted weakly against Latvia, but both finally moved to clamp down on their banking systems as they had developed in the 1990s intertwined with the shadow economy, closing over half of banks in both countries. The results of the US intervention in 2018 was to make a "corpse" of the offshore sector, since, for Latvia, failure to close the offshore sector as required would have put the country's entire US-based strategic security at stake.

Retrospectively, respondents largely agreed that AML failed in Latvia because regulators had close informal relations with bankers, and banks derived their business precisely from the sabotage of AML rules. Thus, we can say that one of the defining features of Latvia as an OFC was the informal ringfencing of non-resident banking from AML. However, this should not be equated with complete capture of the regulator by the banks. As described in Chapter 5, from the 1990s onwards Latvian financial regulators inspired by the the Chicago School economists pursued laissez-faire policies regarding banking regulation, which extended to AML and became the basis for Latvia's 'onshore offshore' status down to 2018

Finally, I considered the question of 'what comes next?' - whether the Riga offshore assemblage has expired or regrouped after the US intervention. Chat groups point to EMIs as potentially being a new chapter in the story of offshore Latvia

Chapter 9. Conclusion

9.1 Main results

This thesis has argued that Latvia emerged as an offshore centre that specialised in the shadow economy of the CIS states, i.e. a shadow-economy OFC, which might also be termed a money-laundering hub. While there is frequent mention of money laundering in the literature on offshore finance, there have been few studies of an offshore financial centre specialised in money laundering. In this conclusion, I will first summarise the empirical results pointing to Latvia's extensive money laundering activities, before recapitulating how these were facilitated by Riga's being effectively whitelisted as a jurisdiction with high AML compliance and reputation. After summarising my theoretical arguments around the term 'assemblage', and considering the research results in the light of ESRC research priorities, I will make some concluding remarks.

My analysis of 213 criminal investigations involving foreign banks in Ukraine, the second largest CIS country after Russia, showed that Latvia dominated the market in financial transactions linked to crimes between 2007 and 2017. Nearly three quarters of all investigations of economic crime involving foreign banks handled by Ukraine's courts involved clients of Latvian banks exclusively or in combination with clients of other foreign bank jurisdictions. Over half of all non-Ukrainian firms - over 500 in total - involved in economic crime in Ukraine banked in Riga. Latvian bank clients were three times more involved in criminal investigations in Ukraine than were Cyprus bank clients, the second most frequent banking jurisdiction in criminal investigations, pointing to Riga's predominant position on the market for money laundering.

Analysing the types of crimes involved shows the preponderance of corruption offences, 'laundromat' type operations, and bank fraud. These three categories taken together show that Latvian banks were embedded in Ukraine's political economy as part of the institutionalisation of the shadow economy. Conversely, the profile of clients of Riga banks involved in economic crime in Ukraine is not clearly distinguishable from the overall profile of Riga bank clients. Thus, the Latvian bank clients involved in economic crime in Ukraine can be regarded as broadly representative of Latvian bank clients as a whole. The further analysis of the geography of criminal investigations shows that Riga banks acted as a hub for dirty dollar funds to move out of Ukraine and sometimes back into Ukraine. Where it was possible to establish the final destination of the funds moved via Riga in criminal investigations, this was predominantly the traditional European secrecy jurisdictions of Switzerland, Monaco, Austria, Liechtenstein as well as Cyprus. Funds were moved back into Ukraine for acquisitions or paid out in cash to individuals.

Using a webscraper I assessed the business activities of around 2000 SLPs as a proxy for Latvian banks. The results showed activities with high shadow economy risks: primarily trade intermediaries in import and export operations to the CIS countries; secondly, SLPs with ‘dummy’ websites targeting AML screening software; thirdly, pyramid schemes and ‘scams’ involving binary trading schemes, and high yield investment plans. Therefore, the online profile of SLPs also pointed to the shadow economy activities of Riga bank clients.

Legacy bank data helped examine the operations of ‘laundromats’, part of the informal institutionalisation of Latvia as an OFC. The ‘laundromat’ comprised networks of shell firms operating across multiple banks to pool and move clients’ money in bulk secretly into the global financial system, using redundant payments and falsified documentation, before paying it out to final beneficiary accounts according to client orders. Examining the business operations of ABLV, the largest Latvian offshore bank, identified the ‘laundromat’ business in the bank’s business parameters. Around 13,000 clients were incorporated as shell firms registered in countries permitting high levels of secrecy. This meant that businesses in the CIS states could secretly control firms with bank accounts in Riga and use them for revenues undeclared in the country of origin. ABLV clients conducted over $50bn of incoming and outgoing payments per year in hundreds of thousands of wires. The bank itself produced falsified documentation to legitimise transactions, and defended its clients against queries from correspondent banks, according to FinCEN and interviews. Thus money laundering was institutionalised in the largest offshore bank’s operations.

Whitelisting, or onshore offshore

Latvia’s success as an OFC was based on the fact that it was not one, according to regulation-centric definitions of OFCs that refer to ringfencing, low tax regimes and secrecy of corporate ownership. It was an ‘onshore offshore’ financial centre: de jure onshore, while de facto offshore, and thus ‘flew under the radar’ of heightened international scrutiny of offshore finance. In terms of banking regulation, Latvia was characterised by deregulation of currency and domicile of bank clients, rather than by regulations on low tax and corporate secrecy. This opened up the banking system to non-residents, predominantly shell firms domiciled in secrecy jurisdictions, holding dollar deposits. Therefore, Latvia avoided classification as an OFC and the concomitant heightened scrutiny, while in fact hosting a large offshore banking sector.

Secondly, there was informal ringfencing of the non-resident sector from application of AML regulations, which I have described as banks' 'sabotage' of AML. Interviews with regulators, bankers and investigators, and examination of chat forums of offshore practitioners, revealed that while on paper Riga had excellent best-practice AML laws, these were systematically not enforced. Lack of enforcement was attributed on one hand to the underfunding and understaffing of institutions such as FIU and FCMC, on the other hand to informal and corruption networks between offshore banks and regulators, as well as a declared government policy of support for the offshore banking sector described above, including regulatory support for its reputation. Thus, Latvia fitted into a pattern described in the literature as typical for OFCs, of good implementation of AML institutions as a reputational measure, but without enforcement by regulators and deliberately sabotaged by banks. Banks sabotaged AML controls on behalf of clients, and enjoyed regulatory connivance in doing so. This informal ringfencing of the offshore sector from AML effectively reprised the "Seychelles strategy" of actively competing on the global money laundering market, and comprised the competitive advantage that caused Latvia to become a major shadow economy OFC, i.e. a money-laundering hub, which was facilitated by Latvia's overall good standing within the FATF network.

Thirdly, building on the above, Latvia's offshore banking sector and regulators referenced the enactment of AML legislation along with EU and NATO membership to claim that Latvia was part of "Western civilisation" and so entitled to US dollar clearing (FCMC 2015a p6). Latvian banks could count on strong political support from regulators in Latvia and from the government due to the geopolitical significance of Latvia as a NATO frontline state against Russia, coupled with concerted lobbying in Washington DC. At the same time in Europe, thanks to the strong presence of Scandinavian banks on the Baltic market, Latvia's joining the Eurozone, and the overall importance of Latvia as one of the few successfully democratic post-Soviet states, there were few questions asked about the activities of offshore banks in

Riga. Latvia's government held such a high reputation in the EU that Latvia's prime minister 2009-2013 took the post of European Commission's vice president for the Euro in 2014, later taking on the European Commission's financial markets and AML portfolios as well. This made Latvian banks a powerful money laundering facility because it provided the legitimacy that money launderers seek to reference for their clients' undeclared money. Thus alongside deregulation and informal ringfencing, whitelisted legitimacy was part of the Riga offshore assemblage.

This whitelisting of Latvia despite the money laundering activities of its offshore banks was replicated in the role of 'prestigious' shell firms incorporated in onshore jurisdictions such as the USA, New Zealand, and the UK. These were engineered to provide equivalent levels of secrecy and tax neutrality as offshore vehicles, but with the reputational advantage of being onshore. Like Latvia's private banks, these legal structures were thus offshore wrapped inside onshore packaging. The prestigious shell firms garnered the reputational bonus associated with the UK, USA, and New Zealand, supporting thereby their shadow economy activities. The money laundering activities of Latvian banks resulted in successive cycles of scandal and reform in USA, NZ, and UK, but this only came home to Riga in 2018, when the US moved to close Latvia's offshore banking sector.

Theoretical findings

My theoretical approach followed Saskia Sassen's discussion of the term 'assemblage'. Assemblages for her are "formations that bring together elements of established fields that usually do not mix," while "discovery rather than replication is my modus operandi (…) assemblage for me is a working category, a tool, not only an outcome, a result" (Aneesh 2017 p129). In my analysis I followed Sassen's advice to use this understanding of assemblage to "actively destabilise existing categories and definitions" (Aneesh 2017 p129).

Sassen's assemblage approach of tracing out heterogeneous networks to destabilise accepted categories proved fruitful for my research. My starting point in tracing and destabilising the assemblage of Riga offshore banking was to interrogate the conventionally perceived relationship between anti-money laundering and money laundering, which sees the former as a response to the latter. Destabilising money laundering by looking at it through the prism of performativity, we can see that money laundering references AML, in that money launderers try to feign AML legitimacy. I assessed Latvia's early implementation of AML as attractive to money laundering, since it lent legitimacy to shadow economy money moved via Riga. Secondly, I interrogated the "banks for non-resident depositors" or "private banks" that comprised the offshore sector in Riga. I established that their business model was not deposits, but channelling dollar payments between the CIS shadow economies and the global financial system. Thirdly, I examined the clients of the offshore sector, who were conventionally regarded as being businesses and individuals from CIS countries attracted to Latvia by knowledge of Russian language and proximity. In fact, while their money originated in the CIS countries, customers were formatted as offshore shell firms registered in secrecy jurisdictions or jurisdictions such as UK that provided a high level of corporate secrecy. Thus bank customers were not exterior to the bank sector, but actants within the assemblage. These shell firms were organised by shadowy para-bank structures that also acted as marketing departments for Latvian banks in the CIS countries. Networking the banks with these semi-legal 'business introducer' structures also destabilised the banks' claims to AML compliance.

Fourthly, I destabilised Latvia as a financial centre by tracing the Riga assemblage into the past. This enabled to me trace 'laundromat'-style banking back to post-Soviet banking in the 1990s, exemplified by the BoNY 'global custody system' involving spinning and fake documents (*prokrutki* and *konformashka)*. Networking Latvian offshore banking with the history of US correspondent banking in the former Soviet countries destabilised the centrality of Riga, by showing that the marriage of US correspondent banking and post-Soviet shadow economy predated Riga's centrality. By tracing the assemblage into the past, it was possible to define 'money laundering' as integration of the CIS shadow economy into US correspondent banking. Fifthly I traced the potential future of Latvian offshore banking, by analysing chat groups of offshore practitioners in the aftermath of the closure of the Riga offshore sector by the US in 2018. Here I noted the incipient 'rewiring' of Riga offshore finance from the correspondent banking model to EMIs and fintech. By introducing this future dimension to Saskia Sassen's conceptualisation of assemblage, I opened it up to rupture and potentiality (Muller and Schurr 2016).

Finally, I destabilised the FATF regime itself, by showing how the FATF regime, intended to combat money laundering, was made complicit in it. Instead of, in Sharman's terms, its bark being its bite, Latvian offshore banking became Sherlock Holmes' "mystery of the dog that didn't bark in the night" because it mistook an intruder for a friend. It took the overriding of FATF by the US sovereign, as 'deus ex machina' to shut Riga offshore banking down in 2018. The US sovereign stepped out from behind FATF to intervene directly in its own interest.

The FATF governmentality regime was thus coopted into the business of integrating the CIS shadow economy into global banking. As we have seen, the implementation of FATF in Latvia went hand in hand with a surge in the amount of dollar transactions via Riga, so that post-2010 as much as 1% of total daily US dollar transactions in Swift were cleared via Latvia. These dollar transactions related overwhelmingly to the CIS shadow economy, and thus can be termed money laundering. While scholars have to date dwelled on the intrusiveness, unaccountability and expansiveness of governmentality regimes such as FATF, this analysis points to the intrinsic weakness of the FATF regime, in particular the reliance on the banking sector to police itself. Extending governance functions to the private sector results in an arbitrary regime that while being intrusive and unaccountable to the weak, is easily subverted by the powerful forces it is intended to subjugate, as I further discuss in the next section.

Findings for the UK banking sector

One of ESRC's five research priorities for 2016-2020 was to reflect on "long-standing criticisms of the economics profession, and particularly mainstream academic macroeconomics" because of the "limited relevance of mainstream macroeconomic theory to associated policy debates" affecting the banking sector. The impetus for such discussion was the "perceived failure of macroeconomists to anticipate the 2008 financial crisis and the subsequent recession" (RCUK 2016 p15).

Banking 'sabotage' of regulations has been argued to have been one of the causes of the 2008 crsis (Palan and Nesvetailova 2020). This thesis also confirms the argument that bankers sabotage regulations to achieve super-profits, in view of the active role of Latvian bankers in sabotaging AML rules and institutions, thereby abusing the responsibilities bestowed on bankers to combat money laundering in the FATF system. This applies primarily to the Riga bankers who acted as 'black sheep' rather than 'big brothers' by defecting from the AML regime. However, it also relates to international correspondent banks who gorged on the ‘remunerative risk’ of integrating the CIS shadow economies and were only dissuaded from doing so by coercive action from the US in the form of the threat of enormous fines (interview #29 British AML officer). Such ‘sabotage’ lies in the nature of banking, where innovation is the driving force behind banking expansion, including innovative methods of circumventing regulation (interview #26 UK academic).

Several respondents expressed doubt about whether the current system of reliance on banks to monitor their customers’ behaviour is viable. In particular, the comparison with telecoms companies is pertinent. Phone providers are obviously not required to monitor client conversations but to provide access for such law enforcement monitoring when required (interview #26). A second point is that for banks, in contrast to credit risk, AML risk is remunerative: banks lose money by pursuing tough AML risk policies and earn money being lax about risk (interview #29 British AML officer). Thus reliance on banks to implement AML is flawed.

> The long-accepted view that such a significant amount of criminal law enforcement should be left in private hands is wrong. Instead, the government should undertake the key role financial institutions currently play in deciding if their clients are possible money launderers or terrorists. (Gordon 2011 p562)

One unexpected research finding is derived from the role of UK shell firms in Eastern European shadow economy activities. My research has shown that these are widely used in money laundering via Riga thanks to their whitelisted onshore characteristics, while providing a high level of secrecy and tax exemption when used with nominees. UK’s streamlining of its company incorporation laws, intended to lower barriers to entrepreneurialism, has made it easy to abuse such structures for the shadow economy operations I have detailed above. Whether use of UK legal entities for shadow economy operations ends with the closure of Riga offshore banking and the introduction of UK reform measures in corporate law is still too early to say.

However, one positive result of this study for UK banking was that these money laundering shell firms incorporated in the UK are not connected with the UK financial sector. UK banks did not feature in my analysis of hundreds of UK shell firms involved in money laundering investigations in Ukraine 2007-2017. Thus, the widespread use of UK shell firms does not imply a major role of UK banking sector in general as a hotbed of money laundering, as is often assumed in press reporting and public discussion. Instead, European offshore banking centres such as Switzerland, Austria, and Cyprus were the leading destinations of money routed via Latvia using UK legal entities. In this way, as ESRC supposes, "[s]ocial scientists often challenge common-sense assumptions about the world, demonstrating the importance of gathering detailed evidence before reaching conclusions" (UKRC 2016 p6). It also means that the UK financial sector's reputation suffers *unjustified* damage as a result of lack of stricter regulation of Companies House.

9.2 Reflections on the research process

As discussed above, one of ESRC's priorities for 2016-2020 was to "[e]xplore the potential of new forms of data (both quantitative and qualitative), and innovations in data collection, linkage and use" (RCUK 2016 p15). The methodological contribution of this thesis has been to use digital data for the qualitative study of human geography, triangulated with traditional qualitative methods such as interviewing. I mobilised four digital datasets taken from the four different access modes of the Internet - surface web, deep web, social web and dark web: a web scraper, a digital archive, a chat forum and leaked bank data. These datasets allowed me to develop proxies for shadow economy activities of Latvian banks: the online activities of Scottish Limited Partnerships (as Riga bank clients), the activities of Riga bank clients in Ukraine, the activities of offshore 'fixers' and of correspondent banks. Taken together, mobilising these digital data sets gave me a rich body of knowledge of Riga offshore banks independent of interview respondents. However, it was also important to triangulate these data with the data gleaned from interviewing.

A further advantage of digital data in this specific case derived from the restrictions on interviewing advised in view of the ethical and other risks connected with the sensitive topic of money laundering, organised crime and state corruption. These risks were seen as significant during ethics review in the context of increased violence against anti-corruption researchers and activists, including the unpunished contract killing of a figure in the immediate research field in May 2018. These difficulties restricted the scope of interviewing, and the pandemic of 2020 additionally restricted interviewing.

Interviewing in fact also became in a sense 'digital data': Because of the ethical and safety risks deriving from the sensitive research topic, I was advised to interview remotely rather than in-person wherever possible. Given the restricted time available for interviewing because of the delay in getting ethics clearance, this proved to be advantageous in providing me with more flexibility over interview times and locations. Moreover, as the Sars-2-Covid pandemic prompted a global lockdown in 2020, the remote interviewing strategy became 'the new normal,' meaning that the new circumstances did not unduly disrupt the chosen research strategy.

Thus, in retrospect I should have pitched a remote interviewing strategy from the outset, which would have accelerated the ethics approval procedure and left more time for interviewing. As a result of the final interview phases partly overlapping with the writing phase, however, in the later phases of interviewing I was able to circle back on questions that seemed particularly pertinent or still unanswered. As discussed in Chapter 4, remote interviewing may lose some emotional nuance, but given that interviews were stipulated to focus on process, rather than persons, for this research project this concern was not of great importance.

The US intervention in Latvia's financial sector in 2018, when the research project was already underway, meant that the position of the US towards offshore banking in Riga became suddenly pertinent. Thus, regarding sampling of respondents, the main deficit was voices from US officials about Latvian banking and the 2018 intervention. My respondents included four former bankers / AML officers at US correspondent banks, but only one individual from US law enforcement. In retrospect, given the restricted onsite access resulting from the lengthy ethics procedure, the research would have benefitted from at least a reading knowledge of Latvian. However, thanks to automatic translation tools in combination with access to electronic archives and help from Latvian colleagues, it was possible to negotiate the relevant primary and secondary literature in most cases. Excellent knowledge of English across Latvia's financial and public sectors prevented my lack of Latvian hindering interviewing, with Russian as a backup.

9.3 Concluding thoughts

In this thesis, I describe Riga as an offshore hub for integrating the post-Soviet shadow economy into US correspondent banking and the SWIFT system. Riga banking was technologically advanced, starting in the 1990s with the introduction of BoNY's microca$h system, and then internet banking. Riga offshore banking, being focused on payments, thus anticipates the current explosion of fintech, particularly in the form of the proliferation of EMIs. This trend sees the payment business being established as a separate industry segment.

The current fintech trend comprises in large part the shift away from correspondent banking as the main payments system towards electronic payment systems and blockchain.

> Correspondent relationships are currently exposed to fundamental changes in the financial sector - despite resilience and almost unchanged procedural structures over centuries - mainly driven by technological advancements connected to the so-called digital revolution. Numerous protagonists of the existing correspondent banking community would even call the latest developments existential threats (…) SWIFT risks becoming a disintermediated intermediary (Guttenberg 2019 p383)

The author of these words, a German politician, was a lobbyist for a leading German fintech company, which collapsed in 2020 in connection with fraud and money laundering allegations (Financial Times 2020). This suggests that digital payment systems may be just as vulnerable to moral hazard as correspondent banking, a concern referred to as the "dark side of digital financial transformation" (Buckley et al 2019).

The story I have told about Riga offshore banking reveals two things about money laundering and high speed electronic payments that confirm such worries. Firstly, the institutional threshold for payment systems as opposed to lending operations is low, and thus electronic payment systems or transaction banking are a channel for mobilisation of shadow economies for the global financial system. Secondly, because of the speed of payments, electronic payment systems have their own inbuilt laundering mechanism, which is the proliferation of redundant payments, obscuring the trail of money from law enforcement. Therefore, Riga's role in the CIS shadow economy is likely to be replaced not necessarily by another centrality as much a different technology. Russia and Ukraine for instance have the world's highest level of adoption of cryptocurrencies measured by size of economy and population, with analysts also noting "the unique role crime plays in Eastern Europe's cryptocurrency economy" (Chainalysis 2020).

This thesis has been a case study of how the FATF regime failed to stop illicit financial flows in a situation where it was best equipped to do so - being embedded in a wider context of good governance such as the EU. Instead, illicit dollars flows accelerated on Latvia's implementation of FATF and accession to EU and NATO. The more that Latvia became well-regarded and compliant, the more it became attractive to post-Soviet US dollars. FATF used normalising reputational leverage - the threat of naming and shaming - as its main mechanism to achieve fast rollout worldwide. Given that money laundering is a question of feigning legitimacy, FATF seems vulnerable to being gamed by money launderers who structure dirty money geographically so that FATF legitimises it rather than sanctions it. The FATF's regime's reliance on the profit-driven private sector for enforcement is another major vulnerability.

There has been frequent criticism of FATF as ineffective after egregious money laundering cases. This thesis has been an exploration of why FATF failed in one major case of systematic centralised money laundering of kleptocratic revenues, via Riga, finally requiring direct intervention from the US to close laundering operations. I found the answer to lie in Riga's reputation and status as an area of good governance, clean money and FATF compliance, combined with deregulation and regulatory connivance with local banks' sabotage of AML regulations, effectively ringfencing the sector from AML. The governmentality regime used by FATF to expand quickly worldwide, but criticised for unaccountability and arbitrariness towards the weak, was in turn found weak when confronted with major concerted money laundering efforts, becoming more an accomplice to money launderers than a hindrance. These findings thus show that there is still too little, or the wrong sort of, institutionalised resistance to offshore finance's facilitation of corruption and the resulting undermining of democracy, beside the sporadic unilateral actions of powerful states.

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