We are pleased to present here our report, **Russia: Illicit Financial Flows and the Role of the Underground Economy.**

This report has been a particularly interesting analysis for Global Financial Integrity. Utilizing the usual World Bank Residual model plus trade misinvoicing yields a figure of US$782 billion in unrecorded outflows from Russia for the period 1994 to 2011. Utilizing an alternative model—Hot Money Narrow plus trade misinvoicing—yields a figure of US$211 billion for the period. What can account for this difference in the two results?

The traditional World Bank Residual model can include both recorded and unrecorded private sector flows. The Hot Money Narrow model focuses on Net Errors and Omissions, that is, unrecorded flows. The difference in the two figures suggests that there has been a great deal of recorded private sector outflows from Russia.

There is a basic difference between legal and illegal flight capital. The legal component stays on the books of the entity or individual making the outward transfer. The illegal component is structured to disappear from the books of the entity or individual making the outward transfer. How much of what appears to be legal flight capital from Russia has in fact stayed on the books of the transferring entities? This is a most interesting question, beyond the scope of this analysis but one we would like to address in subsequent studies.

Another major component of illicit financial flows from Russia does not show up in this study or indeed in our other studies. There are two ways to misprice trade—reinvoicing and same invoice faking. When IMF Direction of Trade Statistics reveal a substantial difference between export and import values of merchandise trade recorded by pairs of trading countries, this indicates that trade has been reinvoiced somewhere between export and import. However, incorporating the mispricing within the same invoice as a matter of agreement between exporters and importers does not show up as a difference between export and import values. Russian companies have aggressively utilized same invoice faking for years. Beginning in the 1990s, many Russian corporations established subsidiaries in Europe to function as buying offices. In addition, hundreds of corporations established their own “pocket” banks to handle their trade documentation and financial transfers. By selling exports to their foreign subsidiaries and by buying imports from their foreign subsidiaries and by utilizing their own pocket banks to handle the transactions, Russian corporations have been able to transfer hundreds of billions of dollars out of their country. None of this shows up in our data or in other analyses of flight capital from the country. Moreover, IMF trade data does not include services and intangibles, so that mispricing in these areas also is not covered in our study.

With these qualifiers, it should be noted that our analysis of illicit financial flows from Russia broadly accords with other analyses done by the International Monetary Fund and by economic scholars.

Another element we have added to this report is an analysis of unrecorded inflows. We have long maintained that economies are damaged by both unrecorded outflows and inflows, neither of which effectively contributes to economic growth or government revenues. We find that our analysis of outflows and inflows together are strongly correlated to Russia's weak overall governance, with the latter feeding back to drive unrecorded flows. Indeed, it is the governance deficit manifest in so many aspects of the Russian state that presents an enormous problem for the nation itself and for its economic and political relations with other nations.

A major part of the work of Global Financial Integrity is unpacking the opaque. Russia is the most opaque economy we have analyzed, and we look forward to deepening our analysis of its economic realities in the future.

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