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Illicit Financial Flows: Conceptual and Practical Issues

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1. Introduction

Neither the abolition of slavery nor the end of colonial rule over African countries has translated into economic affluence, prosperity or comfort for the majority of African citizens. African countries remain some of the poorest and least developed countries, despite owning huge natural resources and the youngest growing population in the world. As Bastian Obermayer and Frederik Obermaier note in their book,

> "Africa is incredibly rich. Half the world's diamond deposits are found on the African territory, along with a quarter of the world's gold reserves, 10% of oil reserves and 9% of gas reserves. And there's uranium, mineral ores, and much more. The population gets virtually nothing from it: the money simply disappears, into accounts of large multinational companies or safes of the elite."[1]

Although African countries receive and benefit from official development assistance, the continent suffers and continues to suffer from a crisis of insufficient resources for development. Research[2] and reports[3] reveal the sheer scale and magnitude of illicit financial flows from Africa that keeps African countries as some of the poorest and least developed countries in the world. The African Union (AU)/United Nations Economic Commission for Africa (UNECA) High Level Panel (HLP) on Illicit Financial Flows (IFFs) from Africa (the Mbeki panel) established that Africa annually loses more than fifty billion dollars ($50 billion) through illicit financial outflows[4].

In this policy brief we seek to show how the current political economy - its rules, systems, structures, culture and practices have not only created a world order that is not only regrettably skewed against African countries in favour of the richer, more developed Western economies but also enables, facilitates and supports the huge illicit financial flows out of Africa. The situation is made worse and debilitating because of the role of co-opted local elites including political leaders, the business class and technical experts as active participants or silent conspirators in managing, and maintaining this neo-liberal agenda. Nicholas Shaxson in his book *Treasure Islands*[5] reveals that "the African curve of the Atlantic Coastline supplies almost a sixth of US oil imports and about the same share of China's and yet, beneath the veneer of great wealth lay terrible poverty, inequality and conflict", intrinsically linked to "a system of corruption linking the French political and intelligence establishments, the French oil industry and Gabon's corrupt ruler, Omar Bongo."

There is a direct link between the seeming inability of African countries to overcome their development challenges and the current global political-economy that promotes illicit financial flows from Africa through sanitised and generally accepted principles, rules and/or practices for conducting world trade and business. The design and application of Double Taxation Treaties (DTTs); the operation of the international tax system; the systems of tax-cutting and financial deregulation; the existence of tax havens, offshore funds and accounts; the practices of corporate tax dodging; the half-hearted strategies aimed at addressing these injustices such as the Organisation for Economic Co-operation and Development (OECD) led investigation on the 'base erosion and profit shifting' (BEPS) process; and the activities of Multi-National Corporations (MNCs); to name but a few, are some of the ways the globalisation project has been conceptualised to undermine any real chance for African countries to meet the United Nations Sustainable Developments Goals (SDGs) and targets.

Efforts to redress this situation remain futile to date. Hence, the importance of persistently flagging up the problem of illicit financial outflows from Africa and raising world consciousness to the injustices towards Africa[6]. As

Abstract

The issue of illicit financial flows (IFFs) is of great significance for many countries looking to mobilize domestic resources for achieving their development goals. The High Level Panel on Illicit Financial Flows from Africa, led by H.E. Thabo Mbeki, brought the issue into the global spotlight, notably since the release of exposés like the 'Panama Papers'. This policy brief elaborates on the conceptual underpinnings of IFFs, its sources and the development costs they generate. Building on the report of the High Level Panel, it provides recommendations to stem IFFs from developing countries.

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Tom Burgis states *"as ever, few have drawn the connection between these countries' [read African Countries] political upheavals and the global industries that feed on their natural resources. But some in the west seem to be awakening to the fact that corruption, like football and finance, has gone global."*[7] In this brief we share our understanding of the unjust system that drains billions of dollars out of the continent annually, and make recommendations and a case for bringing citizens back into the political economy discourse; and to reshape the rigged rules and systems into an effective framework for stemming the huge illicit financial flows from Africa to other regions.

2. Background

2.1 Illicit Financial Flows from Africa and Why It Matters

Illicit financial flows means money illegally earned, transferred or used i.e. illegal in origin, movement or use. This definition adopted by the Mbeki panel is shared by Global Financial Integrity (GFI), a Washington D.C. based research and advisory organisation. According to the Mbeki panel report, this is to distinguish IFFs from capital flight, which is sometimes driven by macroeconomic and governance factors that may be entirely licit. The report of the High Level Panel notes that "this definition avoids complicated explanations of what qualifies as IFFs and debates about whether investors should be allowed to respond rationally to economic and political risk" and further that this definition addressed the "issue of IFFs across the entire breadth of financial transactions"[8].

2.2 Why the Global Focus on IFFs?

For Africa alone the sheer scale and magnitude of IFFs are estimated to cost three to ten times official development assistance (ODA)[9] and the value lost is put at between USD 60 billion to 1 trillion annually[10], up from USD 20 billion in 2001. Estimates show high flows from 33 African countries, amounting to $353.5 billion between 2000 and 2010[11]. There is a disturbing trend indicating increased outflows annually. Other regions are affected too, including rich States like Ireland and Iceland. The European Parliament estimates that European Union (EU) governments lose up to €70bn (£56bn) a year through corporate tax avoidance[12].

The Panama Papers (and recently Paradise Papers) exposés are the largest revelations to date exposing the dark secrets of how the rich and MNCs avoid paying their share of taxes by hiding fortunes in offshore havens. According to these papers, corporations in "*African states avoid paying about $38 billion in taxes, because companies operating there divert their profits to tax havens*"[13]. A statement attributed to Tom Burgis, a British author and Financial Times correspondent describes the situation thus – "*an invisible machine is working to plunder the continent. A looting machine. A coalition of corrupt dictators, unscrupulous large corporations and ruthless banks, all working hand in hand, united in their greed*"[14], with shell companies often used by "*autocrats and corrupt business people … en masse in order to cover their tracks and to invest money abroad*"[15]. The Panama exposé generated outrage around the world over how such nefarious practices, running through a network of secrecy jurisdictions, are rapidly widening economic inequality. These disclosures underscore the urgency of a global solution to this increasingly damaging global problem[16].

Still, IFFs have a higher impact on poor, resource-rich countries in the global South due to the high dependence of their economies on natural resources and primary products, and the greater dependence on tax in comparison to developed economies[17]. Additionally the disproportionate impact on developing countries is because rich countries in the global North are often the destination for the funds lost[18] which thereby enter those economies. Growing social discontent and political unrest due to inequality of income, opportunity and futures is a reality of many in Africa. And yet for governments to be able to fund SDGs and deliver on their human rights obligations to provide public health care, education, water and sanitation, affordable housing and transportation among others, all countries must take a concerted effort to curb these IFFs out of Africa. Tax evasion destroys trust in public institutions and the rule of law, and shrinks the fiscal space for investing in public services, social security and other goods and services. Public funds that are essential to guarantee economic, social economic and cultural rights to all are robbed from the people.

The increased focus on IFFs by governmental and other actors followed the realization of its staggering scale, at a time of economic pressure on many countries associated with the 2008 global financial crisis in Western countries. The scope of IFFs was flagged to African governments at an AU meeting of finance ministers in 2011, which resolved to set up a high level panel headed by H.E. Thabo Mbeki to investigate how to end IFFs from Africa and make recommendations to African governments.

2.3 The High Level Panel on Illicit Financial Flows from Africa (Mbeki HLP)

The HLP on IFFs from Africa was set up in February 2012 by the AU/ECA Ministers of Finance and Economic Development with specific Terms of Reference - to determine the nature and patterns of illicit financial outflows from Africa; establish the level of illicit financial outflows from the continent; assess the complex and long term implications of IFFs for development; sensitize stakeholders including governments and citizens; and make proposals to reverse it. It was chaired by H.E. Thabo Mbeki, former President of South Africa[19].

While exploring the policy dimensions of IFFs, the HLP adopted an approach that matched original research with advocacy and inclusive consultations. To this end the HLP commissioned a background paper to explore the nature, magnitude and development challenges of IFFs from Africa based on disparities in national income accounts and trade data and the extent to which financial secrecy among Africa's trade partners exposes African countries to risk of IFFs through trade mis-pricing or mis-invoicing.

It conducted six country specific studies[20] and consultations with a wide cross-section of stakeholders in and outside Africa including policy makers, private sector and civic organizations alongside an advocacy and communication strategy to create awareness about IFFs and its impact on Africa.

2.4 Key Findings of UNECA High Level Panel on IFFs[21]

1: Illicit financial flows from Africa are large and increasing

• IFFs from Africa increased from about $20 billion in 2001 to $60 billion in 2010.

• IFFs are estimated to be between 3 – 10 times ODA[22].

• This impacts on development including losses in tax revenue, savings and economic investment and undoes domestic resource mobilization capacity that would fill the declining ODA gap.

2: Ending illicit financial flows is a political issue

• The political economy of IFFs is central to ending it – it is driven by highly powerful actors and interests, and has harmful governance effects. Political commitment is key for any action.

3: Transparency is key across all aspects of illicit financial flows

• IFFs are enabled by financial secrecy jurisdictions; in-house trading by MNCs in which information on inputs, outputs, and services is often opaque.

• Transparency in financial reporting requires reforms such as country-by-country account of sales, profits and taxes paid by MNCs; declaration of beneficial ownership in commercial entities, including banking and securities accounts; and cross-border exchange of tax information to cut down aggressive tax avoidance or evasion.

4: Commercial routes of illicit financial flows need closer monitoring

• Commercial drivers of IFFs cause two thirds of losses. They include under-declaration of exported oil, gas, minerals, and agricultural products such as timber and fish. But there is no global regime for commercial IFFs drivers.

5: The dependence of African countries on natural resources extraction makes them vulnerable to illicit financial flows

• The extractives sector is a major area of IFFs. Poorly structured natural resource extraction contracts are used to reduce or eliminate legitimate earnings from royalties or tax.

6: New and innovative means of generating illicit financial flows are emerging

• These bring new twists to the issue, increasing challenges in stopping it.

7: Tax incentives are not usually guided by cost-benefit analyses

• Corruption is a key driver of tax incentives like tax holidays. Studies show no relation between foreign direct investment (FDI) and tax incentives. Real decisions on FDI are influenced by political stability, cost of doing business like energy, infrastructure and labour. MNC tax abuse burdens smaller domestic firms, yet small and medium-sized enterprises (SMEs) contribute more to employment than MNCs.

8: Corruption and abuse of entrusted power remains a continuing concern

• IFFs undermine state institutions, rule of law and state capacities, affecting public confidence and diverting public money to private uses.

• IFFs skew income distribution and are linked to inequality.

9: More effort is needed in asset recovery and repatriation

• IFFs primarily go to external destinations such as tax havens. These are both traditional and new destinations.

• The Tunisian experience post-Middle East and North Africa (MENA) uprising illustrates the role of banks, accounting firms, and lawyers in supporting and enabling MNC practices and outdoing government capacities.

10: Money laundering continues to require attention

• Harmonization of laws on anti-money laundering is required to address criminal acts. MNCs misprice imports & exports to avoid duties or transfer monies, especially foreign exchange out of African countries. Liberia's situation on this is worsened by having USD as legal tender.

• Policies such as de-regulation and liberalization reduce ability of governments to stem money laundering.

11: Weak national and regional capacities impede efforts to curb IFFs

• IFFs reduce capacity of African governments to give essential public services such as health, education and to invest in physical infrastructure. IFFs have a direct human cost especially on the most vulnerable citizens.

• IFFs weaken the financial sector, tax collection, market regulation and integrity of public financial systems, stability and security. Liberalized and de-regulated economies enable IFFs by cutting regulatory capacity of key agencies such as customs.

• Government technical capacity is often insufficient to prevent trade mispricing; support negotiation of good contracts in the extractive sectors, and to monitor resource exploitation.

• Strong negotiating capacity is necessary to shape the emerging global architecture.

• Within Africa as a region, the African Tax Administration Forum (ATAF) has initiatives relevant for capacity building.

12: The global architecture for tackling illicit financial flows in incomplete

• The global architecture is uneven. There are adequate global frameworks on government corruption and criminal activities like money laundering, but not on IFFs from commercial activities.

13: Financial secrecy jurisdictions must come under closer scrutiny

• Transparency, uncovering secrecy and obtaining information, collaboration, cooperation, are key challenges.

• Tax havens and financial secrecy jurisdictions enable easy registration of corporate special purpose vehicles and nominal owners that mask beneficial owners.

14: Development partners have an important role in curbing IFFs

• There are recent initiatives like the Oslo Dialogue on government approach to fighting tax crimes; OECD backed 'Tax Inspectors without Borders' and the BEPS process. But many of these initiatives are not universally applicable or address IFFs from Africa. OECD BEPS agreement omitted major concerns from Africa.

• The cooperation of OECD, the Group of Eight (G8) and Group of Twenty (G20), where most economically powerful states belong and are destination countries is critical to close gaps in global governance on factors enabling IFFs.

15: IFF issues should be incorporated and better coordinated across United Nations processes and frameworks

• The UN should align and prioritize regulation of commercial transactions especially by MNCs and include African IFFs in key global processes like UN post-2015 Development Agenda and the Financing for Development process.

(summary of findings from Mbeki report on IFFs from Africa)

3. Conceptualising IFFs

Illicit financial flows are defined as ***money illegally earned, transferred or used, i.e. illegal in origin, movement or use***. IFFs are the most damaging economic problem faced by the developing and emerging economies as trillions of dollars required in order to reach the SDGs are siphoned off.

3.1 Modalities used in IFFs

The role of multinational enterprises has been identified as a major driver of practices that undermine a fair system. The Mbeki report shows that two-thirds of IFFs (65%) are due to practices of MNCs with trade mis-invoicing as the largest single source. Use of intragroup loans, DTTs, intellectual property rights (IPRs), management fees, unequal contracts, banking secrecy to abet IFFs, evade tax and other dues to States are some of the MNCs' practices[23].

3.2 Sources of IFFs

• Two thirds of the problem: Commercial transactions – 65% IFFs

The Mbeki panel[24] paid significant attention to commercial drivers of IFFs due to its disproportionate scope on the one hand *vis-à-vis* the other two, and the inadequate focus on it in comparison to criminal acts and government corruption. The insufficient focus on commercial drivers of IFFs is reflected in the near-invisibility in the public narrative of the complicity of corporate actors in driving IFFs and inadequate development of legal tools to fight it. At international, regional and national levels more instruments have been developed to fight government corruption such as the UN Convention against Corruption and the AU Convention on Preventing and Combating Corruption and to address criminal acts like money laundering, largely due to its link to terrorism rather than to regulate commercial transactions that support IFFs. Attempts to develop binding legal instruments to regulate corporate activities and increase transparency have consistently been met with strong lobbying and watered down to voluntary guidelines[25]. Given that *"IFFs often leave developing countries through the commercial financial system"*[26] there is need for a spotlight on commercial drivers of IFFs and the role of major banks and financial centres including extra-territorially.

Small and medium scale enterprises typically use mis-invoicing of imports and exports[27] to evade taxes.[28] However, most commercial mechanisms for IFFs lend themselves more to application by MNCs due to their multi-jurisdictional presence and ability to exploit loopholes and divergence in global, regional and national financial rules on double taxation and banking using intra-house trade and special purpose vehicles like shell corporations.[29]

> *"By using complicated tax arrangements, some multinationals can pay nearly a third less tax than companies that only operate in one country. It's not right that smaller companies should be at a competitive disadvantage to multinationals."* (Jonathan Hill, EU commissioner for financial services)[30]

Even advanced economies face challenges tracking the tax dues of MNCs due to lack of country-by-country reporting on profits, taxes, employees, and turnover, leading the EU to push for more transparency and closer regulation of multinational operations with turnover greater than €750m and the OECD to set up a process to curb BEPS activities within its member states.

The Mbeki report and other sources[31] highlight several cases through which commercial IFFs were found to take place in Africa -

• Tom Burgis in his book noted the smuggling of goods ranging from guns to counterfeit products from mostly China across west African countries of Benin, Nigeria to Niger, among others[32];

• Abuse of tax holidays for new foreign investors by hotels in Tanzania through periodic false ownership change, cited in regional consultation for East and Southern Africa of Mbeki panel;

• Unequal concessionary contracts in the mining sector (Guinea)[33];

• Arms smuggling and instigation of armed conflict between war lords to avoid government regulation and taxation (DRC) (cited by women from eastern DRC in meeting on Transitional Justice)[34].

Nicholas Shaxson (2012) writes that by the early 1980s,

'*the main elements of the modern offshore system were in place and … while the old European havens were mostly about secret wealth management and tax evasion, the new British and American zones are mostly about escaping financial regulation with a lot of tax evasion and criminal activity thrown in*'.[35]

• Criminal drivers of IFFs

The second largest source of IFFs is criminal transactions such as money laundering, smuggling and trafficking in humans, drugs and arms. About 30% of IFFs are traced to criminal transactions. While some of the proceeds of criminal IFFs exit through overtly illegal means such as smuggling, a significant proportion is extracted using the same loopholes exploited by commercial IFFs such as rules allowing opaque banking transactions, tax havens and financial secrecy jurisdictions.

• Government corruption

Corruption by government officials contributes 5% of IFFs from acts such as bribery, theft of state assets and abuse of office. However, the acts of government officials are an enabling factor in both commercial and criminal drivers of IFFs, contributing to weak state regulation of business malpractice, unfair concessionary agreements obtained through collusion or aiding and abetting smuggling and trafficking rings by law enforcement, revenue and custom agents. Overall, official corruption by government officials weakens the ability and commitment of the state to fight and contributes to a governance environment conducive to continued outflows.

4. Economic Growth versus Development: An Ideological Concept and Construct

The failures of the current financial system and dominant model of development are self–evident. There are several crises threatening the world's political economy today generated by current global financial rules and systems. For serious reform to happen addressing structural issues, an ideological shift is needed away from the mantra about "***growth***" to the concept of development. The "***growth***" approach to measuring progress is hinged on the neoliberal ideology which through its main pillars of privatisation, liberalisation and de-regulation systematically dismantled the role of the developmental State in promoting inclusive development.

Various authors have sought to shed light on the dominant political order[36]. There are some common threads that run through these exposés and which are pertinent to appreciating IFFs. One is that there is a shadow world in which 'normal rules' regulating the 99% do not apply to the elite, but are reversed, whether on tax justice, transparency in business, criminal accountability, rule of law, *even norms on shame and stigma*. The privileged world of the powerful political and economic elite (primarily from richer nations with subordinated local collaborators from the global South) is a bubble separating and protecting this minority from the rest.

These opaque systems and power relationships are replicated within and between states, in areas ranging from financial, taxation, banking, accounting, law, primarily in matters business and economic that rig key rules or outcomes, for example, on double taxation, in favour of the powerful and wealthy.[37] Global, regional and national financial rules are gamed to favour the wealthy, for example there is often pressure on developing States to apply OECD as opposed to the UN double taxation model; yet the latter based on source of profit is more beneficial than the former based on residence of the corporate entity.[38] Continued protection of banking and financial secrecy of tax havens and offshore businesses reflect this shadow system.

Unwritten rules extend this world to the political and economic spheres creating a nexus between privileged political, economic and social elites, with subtle blurring of principles and a dominant narrative presenting abusive privilege and practice as normal, smart and licit. Fighting this opaque, shadowy system is challenging and dangerous, with those who fight it branded and immense resources made available for supporters of this global regime from States and corporations.

Perhaps the biggest success of the neoliberal system has been conceptual, the successful rebranding of 'growth' as development and entrenchment of its ideological pillars in the strategic centres of decision making in state and global institutions, in the realms of finance, trade and aid.

Every political economy generates its norms, values, orientation and practices. A presentation on the neoliberal moral economy in Uganda that explores capitalism, socio-cultural change and fraud[39] stated that the very fabric of society and specifically values and practices in economics and politics has been re-aligned to the dominant norms and values of a market society; this has transformed Ugandan society and culture, towards '*materialism, self-interest, opportunism, short-termism and corresponding relatively low regards for both others and the common good*'. It reflects a global trend since the 2000s in which neoliberalism has engineered moral restructuring of societies resulting in '*… the new age of fraud where economic deception has become a structural feature of the global economy and an issue of concern in many societies*'.

The effect on elected representatives of the people is to create an invisible constituency that trumps voters and skews even constructive initiatives aimed at reducing inequality: the development agenda in the World Trade Organization (WTO), Financing for Development, the UN SDGs, and the OECD BEPS process. The inconsistency in rules is seen in deregulation of big business as contrasted with increased restrictions on labour and citizens through public order laws, a phenomenon described increasingly as shrinking space for citizens.

The application of neoliberal macro-economic policies through the International Monetary Fund (IMF) and World Bank (WB)-recommended structural adjustment programs (SAPs) in Uganda from the second half of the 1980s to date has led to reversals in all key human/ sustainable development indicators.[40] The mode of implementation, for example, in the privatization of state assets was highly irregular and corrupt, resulting in stripping of public assets by political and business elites and downsizing of public services on which the poor and middle class relied. The effect of so-called market led growth has been growing inequality and growth without inclusive development.[41] De-regulation led to the shrinking of state regulatory structures, particularly those protecting labour and social services; introduction of so-called market and investor-friendly policies has further tilted the balance towards powerful commercial actors – often fused with political elites - and fragmented the organizing and bargaining power of citizens. Anti-poor state policies and practices have often brutally suppressed and led to the demise of citizen-organizing through people's organizations[42] - cooperatives, trade unions, professional and trade associations and the like. The outcome of the neo-liberal political economy has been State capture, progressive gutting of State capacity, reduction in the will to regulate powerful individuals and corporations, and proliferation of all three forms of IFFs.

IFFs are enabled by the neo-liberal policies of privatization, liberalization and de-regulation and the imposition of aid conditionalities to access international concessionary financing. Studies show that the neoliberal model has transformed economies and deepened inequality within and between countries and regions, with the rich getting richer and the poor, poorer.[43] The effect of neo-liberalism, the latest face of globalization in Africa is the paradox of a highly endowed continent, rich in resources with a largely impoverished population underperforming against all sustainable development indicators. Part of the explanation rests in illicit financial flows and the rigged rules and structural drivers of inequality rooted in the global political economy that enables it. MNCs have been identified as a major driver of practices that undermine a fair system.

The outcome of this growing inequality is an explosion of citizens' disaffection particularly over the inability of political systems to level the ground. Pushed to the wall, citizens of poor, developing and developed nations are increasingly targeting their frustrations on governments as other available avenues for organizing close off. Loss of faith in the elected politicians' commitment to represent majority citizens' interests against elite minorities underlie recent outpouring of people power such as the Arab awakening in the MENA region, Fees must fall campaign and Marikana incident in South Africa, Black Monday movement in Uganda, Occupy movement in several western states and even growing populist nationalism in richer countries as seen in Brexit in the UK and rejection of many mainstream politicians and parties in the USA, western Europe and India.

Legal and competency gaps

IFFs is a complex, highly technical issue and requires a range of tools and knowledge from a range of disciplines such as law, finance, revenue and accounting to comprehend. Though topical today, IFFs are not widely understood by legislators, technocrats in revenue services, customs and law enforcement officials, judicial officers and various professionals including lawyers, accountants, journalists and bankers. Few development actors have the expertise to address it; neither do ordinary citizens. And yet there is already significant technical expertise and knowledge on matters of taxation, finance and law within African actors, both state and non-state. This presents opportunities to effectively address and end IFFs from multidisciplinary angles.

Interestingly, the nexus between powerful economic and political elites that facilitate and grow from IFFs also lend themselves to criminals and to links between organized crime networks, big business and political officials[44]. Ending this network of powerful vested interests and dismantling the political economy of IFFs is a high stakes game.

5. IFFs Development Cost

IFFs are a human rights issue, undermining *inter alia* the right to development. IFFs' development cost is compounded by low asset recovery and slow repatriation of funds lost, due to intransigence of receiver states, banks and individuals. IFFs have been linked to human rights abuse associated with conflict minerals in a range of cases in several African states from Angola, Algeria, DRC, Guinea, Liberia, Nigeria, Sierra Leone, Uganda, and South Africa to Zimbabwe[45]. The same pattern holds in other regions from Latin America to the Middle East, Eastern Europe and even North America.

IFFs challenge the concept of sustainable development and protection of the common wealth. They cohere to the exclusionary, individualistic and extractive neo-liberal economic model which is causing huge, inadequately compensated losses to countries and communities for natural resources like oil, gas, minerals, and agricultural products like timber and fish[46]. IFFs perpetuate income inequality between countries and between the rich and the rest.

A 2013 GFI study[47] found that IFFs surged to US$ 1.1 trillion in 2013, with $7.8 trillion cumulatively from 2004 to 2013 coming from developing economies. The study found that trade fraud is responsible for $6.5 trillion of the illicit outflows; that IFFs average 4% of the developing world's gross domestic product (GDP), with sub-Saharan Africa still suffering the largest illicit outflows as a percentage of GDP, at 6.1%. Further, in seven of the ten years studied, global IFFs outpaced the total value of all foreign aid and FDI flowing into poor nations[48]. As the GFI report, and indeed others, underscore, IFFs are a growing global problem impacting countries in the global south and north, and both poor and rich countries, but with disproportionate impact on developing and emerging economies due to a variety of factors.

IFFs undermine the role of the state as a development actor, causing huge tax revenue losses and lowering domestic resource mobilization (DRM) in both developing and now-rich states. The threat posed by IFFs to achieving DRM and the SDGs is reflected in goal 16.4 of the SDGs which specifically calls on countries to reduce IFFs by 2030. Developing countries' ability to achieve a stable tax base is significantly undermined by IFFs[49]. The OECD conservatively estimates that 4 - 10% of global corporate income tax revenues are lost due to BEPS, costing the world economy hundreds of billions of dollars a year[50]. Despite evidence that tax competition and incentives are not evidence-based[51], governments desperate for foreign investment cede regulatory control and power to large corporations, who then maximize profits and do not meet their fair share of responsibility to the economy, placing an unfair tax burden on small and medium enterprises and citizens. Failure of large commercial entities and rich individuals to meet their fair tax burden and their illicit transfer of their profits and wealth through IFFs unfairly shifts the tax burden to smaller economic actors and ordinary citizens.

The EU Commission estimates that multinationals pay up to 30% less tax in the EU than rival companies which do not operate across border[52]. Differences in income and corporate tax rates further increase the income gap. Data analysed by Reuter[53] showed that five of the world's largest investment banks, including Bank of America and Deutsche Bank, paid no corporation tax in the UK in 2014.

IFFs are a governance issue, contributing to increased systemic crimes and development of crime syndicates of corporations and corrupt officials including elected representatives[54]. Proliferation of practices such as under-declared exports, smuggling, and unequal contracts eventually lead to state capture, abuse of power and predator states. This is seen in the effective lobbying by powerful corporations and their associations, like the US National Association of Manufacturers against proposed EU reforms of financial rules such as new public reporting standards requiring country-by-country breakdown of profits made, taxes paid, employees and turnover in all EU countries and tax havens[55]. Involvement of key professions like lawyers, bankers and accountants in enabling commercial IFFs represents an existential threat to the rule of law and democracy. Many developing country governments cannot match the technical capacity of these hired hands in negotiations or legal suits involving multinationals.

IFFs incentivize opacity in financial transactions through growth of tax havens and financial secrecy jurisdictions, and use of mechanisms such as special purpose vehicles. They have driven harmful global financial policies and due to the fierce lobbying of vested corporate and rich-State interests, have subordinated the international and democratic rule-making role of the UN in taxation, development, trade, among others. In this situation, international rule-making is increasingly corporate-driven in spaces like the OECD and international financial institutions (IFIs), which are dominated by rich countries, resulting in uneven rules that do not balance the interests of all countries[56]. Rich countries and international power centres like IFIs and the OECD should support international cooperation in international norm setting and respect rules and practices that create equality of decision making in multilateral spaces. The central role of multilateral institutions under the UN system in development of global norms and new rules on taxation and trade among others is critical and is in the global interest.

6. Ending IFFs: From Rhetoric To Practical Steps

The Mbeki report made several recommendations addressing the commercial, criminal and corruption components of illicit flows; these include recommendations to criminalize trade mispricing through strengthened regulation and taxation of corporate entities and transparency and exchange of information on trade transactions data and measures to curb transfer pricing such as investing in institutional capacity of revenue agencies.

In summary, the recommendations indicate the need for governments, intergovernmental bodies and regional blocs to institute measures to:

1. Improve governance and accountability to all citizens, for example, ending opaque and deliberately badly structured resource extraction contracts that deny African countries legitimate earnings from royalties or tax;

2. Strengthen regulatory capacities including resourcing of tax, customs, immigration, and other administrations, to end practices like under declaration of quantities of exported goods;

3. Promote global cooperation and transparency to stop aggressive tax avoidance and trade mispricing in trade imports and exports through cross-border exchange of tax information, country-by-country account of sales of, profits of and taxes paid by multinational corporations, declaration of beneficial ownership in commercial entities, including banking and securities accounts;

4. Support international cooperation in regulatory law reform and systems such as harmonizing anti-money laundering laws and DTTs to avoid double *non*-taxation; and

5. OECD governments must sign up to more measures against tax avoidance, support efforts by African governments to enforce compliance by corporations and make the BEPS process work for developing countries too. The OECD's failure to fully include countries from the developing world in the BEPS negotiations, despite requests from the Mbeki HLP and ATAF among others is a lost opportunity.

Clearly, actions to end IFFs must happen at multiple levels from national, regional to global, take place on many fronts and involve a range of actors.

As IFFs are a technical, complex issue, stopping them requires effective regulatory responses to create the necessary legal frameworks in countries and binding regional and international rules to close loopholes in revenue, banking, accounting, trade, customs, investment and IPR laws *inter alia* that enable particularly commercial-based IFFs. These should extend to regulations governing key professionals such as lawyers, bankers and accountants that play a central role in facilitating such transactions and economic sectors particularly prone to IFFs. Critical traditional and emerging sectors are affected by IFFs. These include extractive industries, the financial sector (banking and insurance), e-commerce, telecommunications, tourism, gaming, and industry intangibles like IPR, brands and sales of companies[57]. Agricultural products and natural resources such as fisheries, rubber and timber are also impacted[58].

Strengthening regulatory capacity requires investment by governments in institutional reforms where relevant and training for customs, revenue, finance, law enforcement and judicial agencies. However, the key gap is political commitment and leadership to prioritize and finance reforms, and to strengthen government institutions and machinery for tax administration, contract negotiation, and investment and trade-related financial leakages. In unanimously adopting the Mbeki report, AU member states pledged national and coordinated continental action.

The key message of the Mbeki HLP is that ultimately ending IFF is political, owing to the elite-power nexus on which IFFs thrive and power of economic and political actors IFFs benefit. Thus it requires high political commitment, for example, to close legal loopholes that enable exploitation of financial instruments by MNCs; to support tax administrations like the Internal Revenue Service (IRS) and Her Majesty's Revenue and Customs (HMRC) to close the tax gaps in the USA and UK respectively with regard to corporate tax payments; and to establish an equally robust global architecture for commercial IFFs as for corruption and criminal IFFs.

There is a consensus that IFFs are enabled by opacity in financial and other practices and rules that allow this lack of transparency. Ending IFFs requires significant focus on MNCs which have been implicated in base erosion practices that shift profits across borders to take advantage of tax rates that are lower than in the country where the profit is made through mechanisms like hybrid mismatches, special purpose entities (SPEs), and transfer pricing. Political will is essential for governments to introduce and enforce transparency in transactions and end financial secrecy by corporations and governments in trade and tax. Establishing measures to end financial secrecy jurisdictions and tax havens requires powerful champions within governments and intergovernmental bodies like the OECD and World Bank to overcome vested interests that continue to undermine reform efforts. The World Bank can easily develop an annual indicator of trade mis-invoicing from data governments already provide to the IMF and UN. It will take genuine, courageous leadership to achieve reforms such as public, disaggregated country-by-country reporting of financial information on multinational corporations by country of origin; harmonization of anti-money laundering laws, and double taxation treaties to avoid double *non*-taxation.

IFIs can advance international cooperation and inclusion in development of new rules to govern all States. Support from IFIs, the OECD and the EU Parliament for the central role of multilateral institutions under the UN system in development of global norms and new rules on taxation and trade, and equality of decision making in multilateral spaces would go a long way to strengthen democratic, inclusive international norm-making.

7. Conclusion

There are real opportunities for the world community to end IFFs. The Seventh Joint Annual Meeting of the ECA Conference of African Ministers of Finance, Planning and Economic Development and African Union Conference of Ministers of Economy and Finance in March in 2014 in Abuja issued a Ministerial Statement pledging to

> "21. ...take the necessary coordinated action nationally, regionally and continentally to strengthen our economic governance institutions and machinery, focusing especially on tax administration, contract negotiations and trade–related financial leakages. (And) …engage with the international community, … on the reform of global economic governance, ...to highlight our concerns regarding illicit transfers, including the question of tax havens."

The adoption of the Mbeki report by the AU Summit in 2015 is only the first step for African governments towards practical action to fight IFFs[59]. This has been matched by action by civil society organizations (CSOs) on the issue. Many CSOs including the Tax Justice Network, ActionAid International, the Southern and Eastern Africa Trade Information and Negotiations Institute (SEATINI), Oxfam are campaigning in many countries for tax justice e.g. 'Stop the bleeding' campaign; some women organizations are part of these networks.

ATAF has made some significant contributions. It identified base eroding issues of high priority to African countries not included in the BEPS Action Plan and led in defining AU states' positions and responses e.g. formulation of new standards in commodity pricing, revisions to Chapter 1, interest deductibility, permanent establishment (PE) status, exchange of information and other aspects of international tax issues.[60]

Some professions such as lawyers under the Pan African Lawyers Union (PALU), various judiciaries, customs and revenue agencies have taken steps to build capacity of key professions.

IFFs are not Africa's problem alone but a growing global threat to human development. Non-African governments have a crucial role to play in stemming them: they can ensure that their jurisdictions are not used as conduits or destinations, support a global norm against IFFs and support existing capacities in African countries to end IFFs. Countries can lead by example and take measures that encourage the transparency and simplicity required to have effective tax systems globally.

Overcoming vested interests of corporates and governments requires an alliance of engaged – and enraged - citizens in both the global south and north. Trade unions, students, the youth, women's groups and civil society should be involved to play active parts in reclaiming and taking back control and decision making from the corporate in matters critical to their livelihoods and human development.

The role of parliaments, non-governmental organzations (NGOs), academia, media and social justice movements is central to simplifying the complex technicalities around IFFs so that citizens impacted by it can understand, mobilize and organize to challenge the drivers of inequality and rigged rules within and between countries. Within countries, lobbying will be needed to achieve political commitment for reform of regulatory and supervisory regimes in both north and south.

Further, global citizens' coalitions will need to pressure governments to realize international cooperation in reform of international rules such as on double taxation treaties. The role of intelligentsia, media and NGOs in exposing and unpacking the practices, false narrative and neoliberal ideological environment underpinning IFFs is equally core. These need to build a grand coalition of social justice actors and peoples' organizations including labour, women, youth, landless movements, anti-corruption activists, media, NGOs, elected politicians and academia to challenge powerful vested interests of corporates and political elite to finally cause change.

Endnotes

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5 Shaxson, *Treasure Islands*, p. 1.

6 Mbeki Report, p. 21.

7 Tom Burgis, *The Looting Machine: War Lords, Tycoons, Smugglers, and the Systematic Theft of Africa's Wealth* (London, William Collins Books, 2015), p. 253.

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[17] SEATINI and ActionAid, *Double Taxation Treaties in Uganda*, pp. 20, 23.

[18] OECD, *Illicit Financial Flows from Developing Countries: Measuring OECD Responses* (2014). Available from www.oecd.org/corruption/Illicit_Financial_Flows_from_Developing_Countries.pdf.

[19] The other Panel Members were Vice Chair: Mr. Carlos Lopes, Executive Secretary of the ECA; Mr. Olusegun Apata, retired Ambassador/Chair, Nigeria (Coca- Cola) Bottling Company; Mr. Raymond Baker, Director, Global Financial Integrity; Ms. Zeinab El-Bakri, former Vice President, African Development Bank; Mr. Abdoulaye Bio-Tchane, former Minister of Finance Benin & Africa Director, IMF; Mr. Henrik Harboe, Director, Development Policy, Ministry of Foreign Affairs, Norway; Mr. El Hadi Makboul, Secretary General, Ministry of Industrial Development & Investment Promotion, Algeria; Mr. Akere Muna, President of the Pan-African Lawyers Union/ Vice President, Transparency International and Ms. Irene Ovonji-Odida, International Board Chair, ActionAid International.

[20] Algeria, Democratic Republic of Congo (DRC), Kenya, Liberia, Mozambique and Nigeria.

[21] Mbeki report, Chapter 4, pp. 63-76.

[22] As per OECD and Tax Justice Network, as cited in Mbeki report, ibid., p. 64.

[23] Ibid., pp. 79-86.

[24] Ibid., Chapter 2.

[25] Some of the measures that have been effectively watered down include UN Guiding Principles on Business and Human Rights, and EU-proposed measures for country-by-country reporting by large companies and to deal with tax havens and financial secrecy jurisdictions. Repeated attempts by the AU, African Tax Administration Forum (ATAF) and various NGOs to have the OECD BEPS process include non-OECD countries and issues were not very successful. The lack of political support of rich governments for a UN DTT model and a democratic, UN-led process to reform the international tax system reflect the same bias.

[26] OECD report, *Illicit Financial Flows from Developing Countries*, p. 11.

[27] Mbeki report, p. 28.

[28] Ibid., p. 37.

[29] Obermayer and Obermaier, Chapter 1, pp. 10-38; Burgis, *The Looting Machine*; Mbeki report, ibid., p. 37.

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[31] Mbeki report, Chapter 2.

[32] Burgis, pp. 61-79.

[33] Ibid.

[34] Also cited in Burgis, ibid.

[35] Ibid., p. 147.

[36] Obermayer and Obermaier; Burgis, ibid.; Shaxson; Naomi Klein, *The Shock Doctrine: The Rise of Disaster Capitalism* (Knopf Canada, 2007), pp. 3-21.

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[39] The presenter Jorge Wiegratz is conducting a study on the neoliberal moral economy in Uganda for an upcoming book.

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[44] Shaxson, p. 147; Obermayer and Obermaier, pp. 67 – 69. See also Klein, p. 15.

[45] Burgis, pp. 1-8.

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