GLOBAL STUDIES

No. 37

KRISTINA FRÖBERG
ATTIYA WARIS

BRINGING THE BILLIONS BACK

HOW AFRICA AND EUROPE CAN END ILLICIT CAPITAL FLIGHT

FORUM SYD POLICY FORUM

BRINGING THE BILLIONS BACK
– HOW AFRICA AND EUROPE CAN END ILLICIT CAPITAL FLIGHT

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INTRODUCTION

"The ugliest chapter in global economic affairs since slavery"

Raymond Baker, Senior Fellow at the US Centre for International Policy and Director for Global Financial Integrity Program, June 2007

"It is a contradiction to support increased development assistance, yet turn a blind eye to actions by multinationals and others that undermine the tax base of a developing country"

South African Finance Minister Trevor Manuel, 2008[1]

"We will crack down on the tax havens that siphon off money from developing countries – money that could be spent on bed nets, vaccinations, economic development and jobs"

UK Prime Minister Gordon Brown, March 2009[2]

Every year between US$ 850-1000 billion disappears without a trace from developing countries, ending up in tax havens or rich countries[3]. The main part of this is driven by multinational companies seeking to evade tax where they operate, and has been called *"the ugliest chapter in global economic affairs since slavery"*[4].

The sum that leaves developing countries each year as unreported financial outflows, referred to as illicit capital flight, amounts to ten times the annual global aid flows, and twice the debt service developing countries pay each year. For each dollar that goes to the developing world in aid, almost US$10 come back to developed countries through illicit means. This money, if properly registered and taxed in the country of origin, could of course contribute to considerable development and make a major difference in the fight to combat poverty.

Despite this, and even though rich countries also would gain from measures to hinder illicit capital flight, many development organisations, parliamentarians and other decision makers in European and African countries are not well aware of the issue. Prominent leaders like Obama, Brown and Sarkozy have made strong statements concerning the problem, and some well-known civil society organisations have done extensive work on it. Nonetheless, illicit capital flight is not yet mainstreamed on the agenda of most of the people working with development that is undermined by these illicit outflows.

Capital flight represents a higher burden in Africa, as a percentage of GDP, than in other regions[5]. At the same time, actions to stop illicit capital flight must be taken by decision makers in both Africa and Europe if they are to succeed. The capital outflow from Africa and the absorption into western economies deserve equal attention and require concerted effort. Through greater transparency in the global financial system illicit outflows can be curtailed.

Development organisations and academics in Africa and Europe agree on the measures needed at the international level to put a stop to illicit capital flight. To end the secrecy that enables it, they for example call for automatic and multilateral exchange of information between tax authorities, as well as imposition of sanctions on tax havens that do not cooperate. Another critical measure would be to require multinational companies to report the profit they make and taxes they pay in each country where they operate. This could become mandatory if it was made part of international financial reporting standards.

There is also a need for specific measures at the country level. Such measure include the building of legal frameworks better suited to address the problem, awareness raising about the links between tax evasion, tax revenue and social services, as well as capacity building of tax authorities.

International cooperation to stem capital flight ultimately has to be dealt with in a representative global body like the UN. For this reason, development organisations in both Africa and Europe call for the UN Committee on Tax Matters to be upgraded with a political mandate and strengthened.

Putting an end to illicit capital flight is an urgent matter of global justice, of bringing the billions back to where they were produced and where they should contribute to the welfare of the people. At the same time, it is a win-win opportunity for Europe and Africa. Nations on both continents suffer from illicit capital flight and the loss of growth and tax revenue that comes with it. Both would gain from transparency that would counteract not just tax evasion, but also illegal trade in drugs, weapons and humans. To make it happen it is time for civil society, journalists, and decision makers in Africa and Europe to join cause.

OVERVIEW OF THE REPORT

The first chapter of this report seeks to explain what illicit capital flight is, its global magnitude, how it happens, and its consequences for the poor in developing countries. The chapter also explores the key role that tax havens play in capital flight. The second chapter reviews the measures that have been taken by Europe and the international community so far to combat capital flight from developing countries, as well as the reactions and actions taken in response to measures advocated by civil society organisations and academics.

In the third chapter, illicit capital flight from Africa and the specific context that it operates in is explored. Effects on the African continent are described. To provide concrete examples, case studies of Kenya, South Africa and Tanzania are presented in the fourth chapter. The chapter 'Illicit capital flight from Africa' and the case studies of Kenya and South Africa are written by Dr Attiya Warris. The case study of Tanzania comes from the Budget Working Group of Policy Forum in Tanzania.

In the final chapter, recommendations by civil society organisations in Africa and Europe are summarised.

The discussion in this report is limited to a compilation of existing data and sources of information available on capital flight. It is not intended as a report with primary data, but instead as a survey and comprehensive compilation of work undertaken so far.

NOTE : Since the formulation of this report an update of the estimations of illicit financial flows from developing countries has been released by Global Financial Integrity. This update shows that in 2008 illicit capital flight from developing countries had increased to between US$ 1.26 trillion - 1.44 trillion. During 2000-2008 Africa was the region with the largest real growth of illicit capital flight, amounting to 21.9 %. Please refer to Kar D and Curcio K (2011), *Illicit financial flows from developing countries: 2000-2009, Update with a focus on Asia*, for these new data.

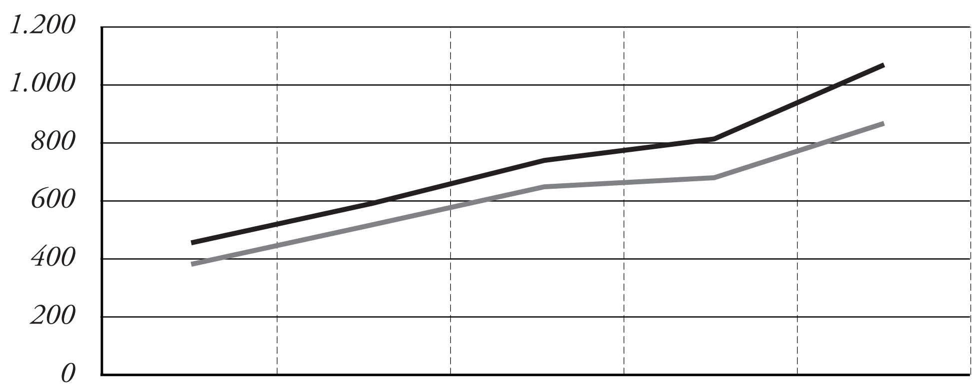
MAGNITUDE, CONTRIBUTING FACTORS AND CONSEQUENCES

By Kristina Fröberg

THE MAGNITUDE OF CAPITAL FLIGHT FROM DEVELOPING COUNTRIES

Illicit capital flight from developing countries are unrecorded financial flows that end up in tax havens or rich countries. (Read more about the definition under the headline definition and origins on page 15.) The most recognised estimations showing illicit capital flight from developing countries and used by, for example, the World Bank, are from Global Financial Integrity, a program at the US Centre for International Policy, which is a non-governmental research institute based in Washington, DC. These show that between US$850 billion – 1 trillion left developing countries as illicit capital flight during 2006[6].

VOLUME OF ILLICIT FINANCIAL FLOWS FROM ALL DEVELOPING COUNTRIES 2002 - 2006 (US$ BILLIONS)



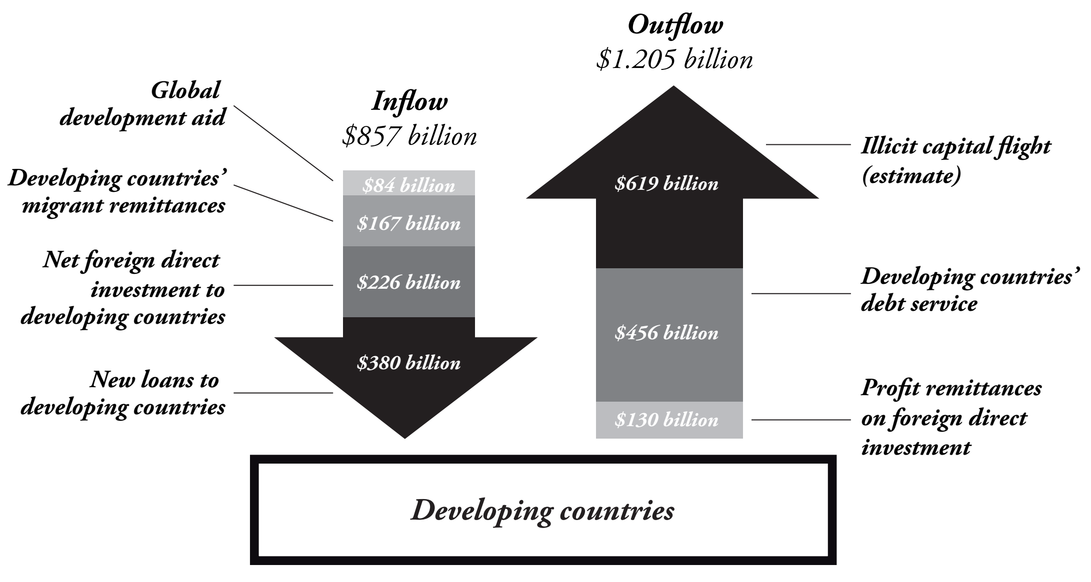
The grey and black lines represent the lower and upper end of estimates of possible ranges of illicit capital flight
Source: Kar, D and Cartwright-Smith, D (2008), Illicit Financial Flows from Developing Countries: 2002-2006, Global Financial Integrity.

Illicit financial flows from developing countries are growing at a rapid and steady pace. Over the 5 year period that estimations were made, the volume increased at an average rate of around 18%[7] per year. Estimations of illicit capital flight from Africa over a 39 year period show that it grew at an average rate of around 12 percent per year.[8]

Multiple economic models and filters are utilized to weed out spurious data in order to yield the most reliable estimates possible. But since illicit financial flows are primarily generated through transactions that completely bypass statistical recording, currently existing models have a limited capacity to reflect the actual volume of illicit capital flight. Because of this inability of official statistics to capture all of the monetary particulars of illegal commerce (which is the driving force behind these illicit outflows) the estimations presented are extremely conservative and are likely to understate the actual problem.[9]

CAPITAL FLOWS BETWEEN DEVELOPING AND DEVELOPED COUNTRIES (AVERAGE 2002-2006)

As shown in the image below, there is a net flow of capital from developing countries to developed countries. Developing countries pay far more on debt servicing than they receive from official donors, and they lose even more in illicit capital flight than they pay on debt servicing. This situation makes developing countries net creditors of donor countries.



Source: Eurodad fact sheet 'Capital flight diverts developing finance'. The image is based on data from the OECD and the World Bank as well as estimates of illicit flows compiled by Eurodad.

EFFECTS ON DEVELOPMENT

Illicit capital flight cancels investment, reduces tax collection, worsens income gaps, hurts competition, undermines trade and drains hard-currency reserves. The flow of illicit money from developing countries is based on shifting the wealth out of the countries where 80 per cent of the world's population lives into countries where 20% live. Raymond Baker, Senior Fellow at the US Centre for International Policy and Director for GFI, calls illicit capital flight "the most damaging economic condition hurting the poor in developing and transnational economies." He comes to the conclusion that for the first time in the 200 year run of the free-market system we have built and expanded an entire integrated global financial structure with the basic purpose to shift money from the poor to the rich.[9A]

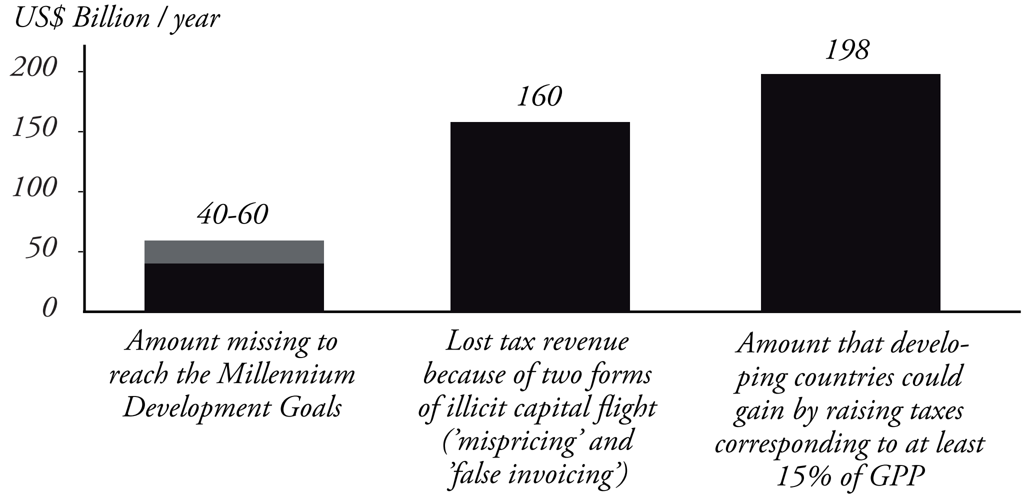
Christian Aid has estimated that due to just two forms of illicit capital flight ('mispricing' and 'false invoicing' by multinational companies, which are explained on page 17-18) developing countries are losing US$160 billion per year in tax revenue. This is more than one-and-a half times the combined aid budgets of the entire rich world, which is around US$100 billion. Taking into account additional sums from aggressive tax avoidance and other forms of trade abuse (which will be defined in the next section), the total loss of tax revenue is several times that amount.

In 2010, more people than ever were going hungry. Almost one billion people were going without even a full meal a day[10]. The United Nations Millennium Development Goals (MDGs) are a set of targets for halving extreme poverty, providing universal primary education, halting the spread of HIV and AIDS, and much more, by 2015. To meet the MDGs, more public sector employees need to be hired, such as teachers, doctors and agricultural extension workers. The World Bank estimates that there is a shortfall of US$40-60 billion per year in the funds needed to reach all of the MDG's. The financial crisis and recession has lowered aid flows, and developing country economies and tax revenues have been affected by declines in external private sources such as foreign direct investments, export earnings and migrant remittances. This has further reduced the chances of meeting the MDGs. If the tax missing through illicit capital flight were paid, there would be enough funds to meet the MDG requirements several times over.

The estimations of revenue lost through illicit capital flight have been made on tax rates that developing countries apply today. Low-income countries – and most middle income countries too – raise a much smaller proportion of their national income in taxes than rich countries. The average for low-income countries as a whole is just less than 15% of national income, but many raise a smaller proportion. In contrast, the world's rich countries raise on average 37%.

A commonly cited reasonable minimum for a developing country's revenue to Gross Domestic Product (GDP) is 15%[11]. At least 21 low and 18 middle income countries raised a smaller proportion than this in 2007. Action Aid has calculated that if these countries had been able to turn at least 15% of their GDP into tax revenues they could have realised US$198 billion more in 2007. This is more than all foreign development assistance combined, and far exceeds the annual MDG funding gap. Economic structures and tax competition discussed later on in this report make it difficult for developing countries to raise their tax revenue, but recent examples from countries like Rwanda, Uganda and South Africa show that it is possible.[12]

AMOUNT NEEDED TO REACH THE MDGs, AS WELL AS LOST TAX REVENUE AND POTENTIAL TAX REVENUE



Source: Estimations from the World Bank, Christian Aid (2008), 'Death and taxes: the true toll of tax dodging', and Aciton Aid (2009), 'Accounting for poverty: how international tax rules keep pople poor'

Not only is tax a potential source of greater funds to invest in public services, it also has advantages compared to aid because of its relatively stable form of income, as well as its close link to better governance and accountability. In addition, it creates an opportunity for greater autonomy on the part of developing countries. Since the amount of aid differs depending on the donor governments elected and the Gross National Income of the donor countries, aid is an unstable source of income. Development aid as a source of income also makes the recipient governments more accountable to donors than to their own citizens. Aid often still comes with conditionalities determining the macro-economic politics of the receiving country, such as privatisation of public services and liberalisation of trade. Hindering illicit capital flight is because of this not only a matter of a country's right to its own resources, but is also important as a democratization process which shifts governments' accountability from donors to its own populations.

On top of tax revenues there are other gains to be made if illicit capital flight could be stopped. If it wouldn't be possible to evade taxes and make big profits on illicit capital flight without getting caught, some of the money might have stayed in the countries of origin. If reinvested, it could have contributed to jobs and growth in those countries.

Illicit capital flight also hurts competition in the free market. The companies that act according to law, and honour their social responsibility through paying taxes, are disadvantaged compared to those that profit from illicit capital flight. Big multinational companies often have more resources than small and medium sized companies to hire lawyers and professionals that could help them pursue illicit capital flight without getting caught. Because of this, capital flight can be a threat to the survival of small and medium sized companies at the national level, as well as to multinationals that report their financial transactions and pay the right amount of tax.

At the individual level, illicit capital flight and tax evasion also create an unequal playing field and worsen income gaps. It is rich individuals that have the means to open an account in a tax haven and place money there without reporting it to their tax authorities. When this is done, tax revenue that could have contributed to social services like health care and education is lost. Both health and education are prerequisites for individuals to raise income. When this cannot be funded by public means, it is poor people that suffer. When national financial imbalances due to illicit capital flight result in devaluation, the wealthy who hold external assets are insulated from the effects, while the poor enjoy no such cushion.

The possibility to conduct illicit capital flight also makes criminal activities like human trafficking and illegal trade with weapons and drugs profitable, and decreases the risk of getting apprehended. Therefore combating illicit capital flight is also a matter of fighting these activities, in other words, tackling human abuse, exploitation and violence.

The same applies to corruption, which in itself is a threat to democracy. If the possibility to pursue illicit capital flight wasn't there, corruption would be less profitable and much easier to detect and trace.

SEVEN REASONS TO COMBAT ILLICIT CAPITAL FLIGHT

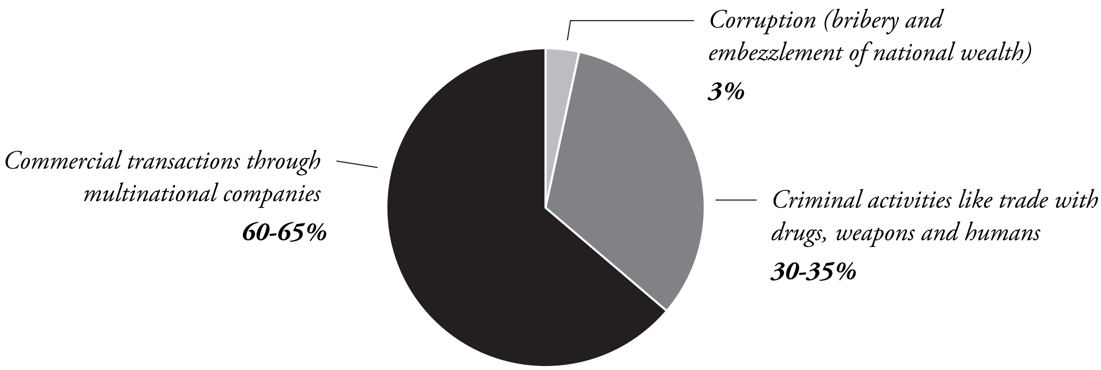
1. ***It would raise revenue incomes and contribute to considerable public funds for development in the countries of origin (typically developing countries).***
2. ***It would reduce the incentive to place profits outside the country of origin, which might lead to increased domestic investments, jobs and growth.***
3. ***It would make criminal activities less profitable and easier to discover and trace.***
4. ***It would make corruption less profitable and easier to discover and trace.***
5. ***It would make governments less accountable to donors and more accountable to their tax payers – their citizens.***
6. ***It would lead to fairer competition in the free market, which would benefit small and medium sized companies at the national level, as well as multinationals that report their financial transactions and pay the right amount of tax.***
7. ***It would reduce income gaps between rich and poor.***

DEFINITION AND ORIGIN

Illicit capital flight from developing countries[13], according to the estimations presented in this report, can be defined as unrecorded financial flows. Flight capital takes two forms. The legal component stays on the books of the entity or individual making the outward transfer. The illegal component is intended to disappear from records in the country from where it comes. Illicit money is money that is illegally earned, transferred across borders, or utilized. If it breaks laws or regulatory frameworks in its origin, movement, or use, it merits the label of illicit. By far the vast majority of unrecorded transnational financial flows are illicit, because they are violating the national criminal and civil codes, tax laws, customs regulations, VAT assessments, exchange control requirements and banking regulations of the countries from which unrecorded/illicit flows occur[14]. For the purpose of this report, the concepts of 'illicit financial flows' and 'capital flight' will be used interchangeably, always referring to illicit capital flight.

Illicit capital flight is comprised of three main types of transactions. The first is arising from criminal activities, such as drug trade, human trafficking and illegal trade with weapons. This part accounts for approximately 30-35% of the illicit capital flows from developing countries. The second is capital flight due to corruption (bribery and embezzlement of national wealth). This accounts for about 3%. The third is commercial illicit financial flows through tax evasion and avoidance practices by multinational companies. This accounts for 60-65% of the illicit capital outflows[15].

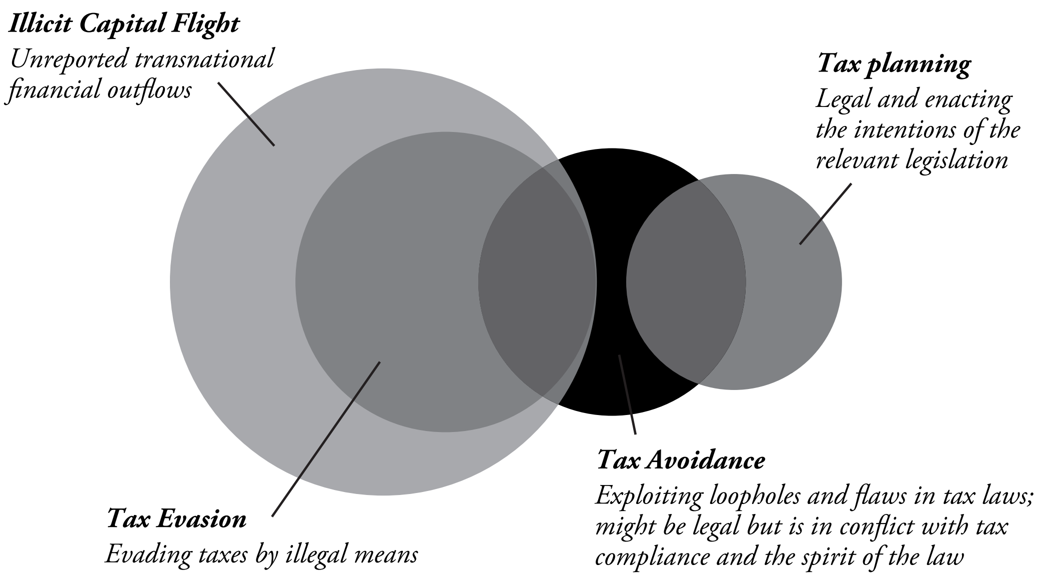
DISTRIBUTION BETWEEN DIFFERENT CATEGORIES OF ILLICIT CAPITAL FLIGHT



Source: Kar and Cartwright-Smith, (2010) Illicit financial flows from Africa: Hidden Resource for Development, Global Financial Integrity, p.1.

Tax evasion is the general term for efforts to evade taxes by illegal means. Tax avoidance entails the legal utilisation of the ambiguities and indeterminacies of tax rules and regulations to one's own advantage, in order to reduce the amount of tax that is payable, by means that are within the law. Aggressive tax avoidance occurs when companies exploit loopholes and flaws in tax laws. Ever more ingenious and complex instruments are invented with the sole purpose of getting around tax laws. Even though this may be legally allowed, such behaviour is in conflict with tax compliance. If a company does not aim to pay the right amount of tax at the appropriate time and place, it abuses the spirit of the tax law. Tax planning is different from both tax evasion and tax avoidance. Any company has the option of carrying out tax planning in order to minimise tax liability within the law of the territory in which it operates. This activity is entirely legitimate in that it is enacting the intentions of the relevant legislation[16]. But between tax evasion, tax avoidance and tax planning there are grey zones.

RELATIONSHIP BETWEEN THE CONCEPTS OF ILLICIT CAPITAL FLIGHT, TAX EVASION, TAX AVOIDANCE, AND TAX PLANNING



HOW COMMERCIAL ILLICIT CAPITAL FLIGHT HAPPENS

Because of the bank secrecy of tax havens, individuals can hide money in them and evade tax simply by transferring money to a bank account in a tax haven, and not inform their country's own tax authority about it. But multinationals, which are large operations with many employees and requirements to report detailed annual accounts on a global level, need to use other methods. The most common methods are described in the following sections.

Transfer mispricing

Multinational groups of companies are often complex structures with hundreds of subsidiaries, a substantial number of which may be located in tax havens where no or very low taxes are paid and secrecy is applied (see explanation of tax havens on page 19). Profits are allocated between subsidiaries through internal trading, a complicated process which is hard for tax authorities to police. It is estimated that 60% of international trade is now intra-firm trade between subsidiaries of the same multinational[17].

Transfer pricing involves determining the sales prices between different entities within a multinational. In most countries this must be done using the 'arm's length principle', that is to say, the price must be equivalent to the open market price that would apply between unrelated and independent companies[18]. Normally, trading parties want to get the best price for themselves. But when two companies trade that belong to the same ownership they do not want the best price for the individual company, but a price that creates the best overall result for the multinational corporation to which they both belong. The companies may therefore allocate the profit between the two subsidiary companies in such a way that a minimal amount of tax has to be paid. When a multinational company deliberately is manipulating the prices they charge for goods or services to artificially high or low prices to shift profits to low tax jurisdictions, this is called transfer mispricing.

EXAMPLES OF TRANSFER MISPRICING

Examples of mispricing are plastic buckets bought by a subsidiary in a developing country for US$973 per bucket from another subsidiary in a tax haven. A more realistic price paid on the open market would have been around one dollar. The rest of the price paid is just a way to shift profit to the subsidiary in the tax haven where less tax is paid.

As an example of a reverse approach, video cameras are sold by a subsidiary in a developing country to a subsidiary in a tax haven for US$13 per camera[19], which is much lower than the open market price. The subsidiary in the tax haven can then sell the video cameras at a market price and the profit made from this will end up in the tax haven instead of the developing country.

Continued on the next page

Transfer mispricing allows even more tax evasion when it is applied to intangibles like logos, brands, consultancies or property rights. The company assigns ownership of its brand in a shell subsidiary created in a tax haven. All the productive parts of the company in other parts of the world then pay royalties and other fees to this shell company. This guarantees a continuous shift of money to tax havens[20].

Global Financial Integrity has estimated the volume of capital flight from developing countries as a result of transfer mispricing. They found that during the year 2006 this amounted to between US$471 and 506 billion[21].

International financial reporting standards (IFRS) only require multinational groups of companies to report on a consolidated basis - that means one set of accounts showing the overall financial activities and results for that group, without breaking them down for each country. This makes it very hard for tax authorities in developing countries to know what profit is made by a multinational company from activities in their country, what tax should be paid, and to uncover evidence of transfer mispricing.

Falsified invoicing

Falsified invoicing could be performed in several ways, all of which have in common that the import or export of goods are not reported truthfully or are even completely falsified. A company in a developing country that is importing goods could inflate the price it declares that it has to pay to the foreign supplier, so that it can report lower profits and therefore pay less tax. The reverse can also happen. A person exporting goods from a developing country could deliberately undervalue what is being sold, at least in official documents, so that profits are once again hidden. Since it is often based on verbal agreements between buyers and sellers, falsified invoicing is difficult to detect and is widespread. It is, for example, estimated that 60 % of trade transactions in Africa are mispriced by an average of more than 11%[22].

Round tripping

Some of the money made from, for example, transfer mispricing, returns to the country of origin through what is called ‘round tripping’. This means that a company that has shifted profits from a developing country towards a tax haven reinvests part of the profits in the same developing country. This time it is being considered as foreign direct investment and thus it can benefit from favourable fiscal conditions like tax holidays offered by the host country. Round tripping allows not only tax evasion and avoidance, but also takes advantage of the tax exemptions that many developing countries grant to incoming investment. Similar ways are also used to recycle money coming from criminal activities into the legal economy[23].

FAILING TAX AUTHORITIES

Another condition that makes illicit capital flight from developing countries possible is that tax administrations often are poorly resourced and lacking in staff capacity. Lack of technology and capacity to collect taxes, as well as the inefficiency and lack of expertise of tax authorities create loopholes that otherwise would have been plugged.

Weak tax administrations and poor tax compliance reduce the tax revenue available to governments, and force them to rely on the taxes that are the easiest to administer, which may not be the most progressive ones. Rich people benefit most from weak tax administrations. These are the people who can afford to put in place tax avoidance and evasion schemes that require time and resources to investigate.

Some of the reasons for the gap in tax efficiency between rich and poor countries are structural. In rich countries, more people are earning above the threshold at which they can afford to pay taxes and still finance their basic needs. Rich countries are also able to raise more tax than poorer ones because a much larger proportion of the economic transactions take place in the formal economy. However, investments in tax authorities' capability have shown significant differences in tax revenue income. Ghana, for example, worked with the German government's development agency GTZ to improve its tax policy and administration between 2003 and 2005. This contributed to an increase in corporation tax revenues of 44% in real terms[24]. International development cooperation to improve the capacity of the Rwandan revenue authority helped to increase tax revenue collected from around US$96 million in 1998 to over US$384 million in 2006[25].

TAX HAVENS

"There is a building in the Cayman Islands that houses supposedly 12000 US-based corporations. That's either the biggest building in the world or the biggest tax scam in the world, and we know which one it is."

US President Barack Obama, December 2007[26]

Tax havens are jurisdictions that use secrecy and low tax rates as a selling point to attract businesses for their financial services industries. The banking secrecy that they apply makes it almost impossible to find out who owns an account there, how much money it is worth, and where the money came from. As a consequence, tax havens also hide criminal activities and illicit flows of money. The Organisation for Economic Cooperation and Development, OECD, (an intergovernmental body comprising the 34 richest countries in the world), describes them as countries that offer themselves as places to be used by non-residents to escape tax in their country of residence.[27] Research based on leaked documents from Lichtenstein suggests that only 5% of individuals placing assets in tax havens declare them for tax purposes in their home country[28].

Tax havens deliberately create legislation to ease transactions undertaken by people who are not resident in their domain. As a result, there is very little activity in tax havens, and they are sometimes described as 'virtual' centres or 'legislative spaces'. Transactions to tax havens can be referred to as 'offshore' because they take place in legal spaces that decouple the real location from the legal location, and legally protected secrecy ensures that transactions are not linked to those who are effecting them. Because of this, tax havens are often also referred to as offshore centres or secrecy jurisdictions. The establishment of tax havens has little to do with geography, such as the misconception that they are typically located on small islands[29]. The term jurisdiction in this context is used to describe any territory with its own legal system. As can be seen on the map on page 22-23, this could be an independent or sovereign state, a component of a federal or confederal state, a dependent, associated or overseas territory, or an internal zone to which a special legal regime has been applied.[30] Indeed, the major global players in the supply of financial secrecy are mostly not tiny, isolated islands, but rich nations operating their own specialised jurisdictions of secrecy.

In the definitions and listings that have been made of tax havens, offshore financial centres and secrecy jurisdictions, there are some differences. The main listings of tax havens have been made by the OECD. In 2000, it identified 41 tax havens using the criteria presented in the box below. In 2007, it was determined that 3 of these should no longer be considered tax havens.

OECD DEFINITION OF TAX HAVENS

Since 1998 the OECD has defined tax havens through a combination of four characteristics:

- ***no or only nominal taxes on relevant income***
- ***lack of effective exchange of information with other tax authorities***
- ***lack of transparency in the operation of legislative, legal or administrative provisions***
- ***no requirement that activity be substantial to qualify for tax residence***

(However, the fourth criterion of 'no substantial activities' was rejected by the new US administration in 2001 and withdrawn in the OECD Progress Report of 2002)

In 2000, The Financial Stability Forum (a group of finance ministers, central bankers and international financial bodies from 12 developed nations) created a list of Offshore Financial Centres largely similar to the OECD list of tax havens, but using different indicators. The World Bank and IMF used this list and expanded it with four jurisdictions, identifying 46 offshore financial centres.

Tax Justice Network (an independent organisation dedicated to research and analysis in the field of tax and regulation) launched a 'Financial Secrecy Index' in 2009. This is a ranking of the jurisdictions that are most aggressive in providing secrecy in international finance. The ranking combines two broad measures, one qualitative and one quantitative. The first measure is an opacity score based on verifiable sources which looks at laws, regulations, cooperation with information exchange processes and so on. This is given most weight. The second measure is a weighting to each jurisdiction according to the scale of cross-border financial services that it hosts. The top ten secrecy jurisdictions in the ranking are: Delaware (USA), Luxembourg, Switzerland, Cayman Islands, City of London (UK), Ireland, Bermuda, Singapore, Belgium and Hong Kong. The index contains 60 jurisdictions in total. Half of them are closely connected to Britain, either through their status as Crown Dependencies or British Overseas Territories, or through membership in the Commonwealth of Nations (formerly the British Commonwealth).

Most of the jurisdictions listed in the Financial Secrecy Index have been defined as tax havens in a list of tax havens which Tax Justice Network released in 2007, using the criteria presented in the box below. This list contains 69 tax havens.

TAX JUSTICE NETWORKS DEFINITION OF TAX HAVENS

- *strong bank secrecy*
- *low or zero taxation*
- *no requirement of economic substance for the transactions booked*
- *ring fence between its domestic regime and the regime offered to non-residents*[31]

In the past 30 years, the number of tax havens has grown rapidly. This rise has been facilitated by technological development that has increased the mobility of financial flows. In 2007, more than half of global trade occurred via tax havens, although these accounted for merely 3% of global GDP[32].

Due to its culture of secrecy, the size of the offshore economy is hard to measure precisely. International efforts to measure it often have focused only on narrow aspects of it. But in 2010 GFI released a report that looks at deposits held offshore by private entities on a country-by-country basis, achieving a level of specificity previously unavailable to the public. The GFI report analyzes data from the Bank of International Settlements and the International Monetary Fund to measure deposits in areas considered as secrecy jurisdictions under the definition established by Tax Justice Network[33]. The total current deposits by non-residents in tax havens is according to this just under US$10 trillion. (If 15% of this would be paid in tax it would raise US$1500 billion, which is 15 times more than total annual global aid). The report also concludes that the rate of growth of offshore deposits in secrecy jurisdictions has expanded at an average of 9 percent per annum since the early 1990s, significantly outpacing the rise of world wealth in the last decade. The gap between these two growth rates may be caused by increases in illicit financial flows from developing countries and tax evasion by residents of developed countries[34].

OECD Countries

Australia
Austria
Belgium
Canada
Chile
Czech Republic
Denmark
Estonia
Finland
France
Germany
Greece
Hungary
Iceland
Ireland
Israel
Italy
Japan

Tax havens, offshore finance centres, and secrecy jurisdictions according to either the OECD-, IMF-, or Tax Justice Network-lists, or jurisdictions ranked by the 'Financial Secrecy Index'.

Classifications according to OECD, IMF and Tax Justice Network, and ranking of the tax havens marked on the map, can be found in the table on page 74-75 in the appendix.

OECD countries are marked with ■ or « if also a tax haven

Korea	*Poland*	*Switzerland*
Luxembourg	*Portugal*	*Turkey*
Mexico	*Slovak Republic*	*United Kingdom*
Netherlands	*Slovenia*	*United States*
New Zealand	*Spain*	
Norway	*Sweden*	

Tax havens are also hosting a large part of the shadow banking system, because of the streamlined regulation that allows financial institutions to circumvent the regulations imposed in other countries. Nobel laureate Paul Krugman argues that the lack of regulation of the shadow economy laid the groundwork for the financial crisis, re-creating the kind of financial vulnerability that made the Great Depression possible[35].

It should be kept in mind that some of the tax havens are located in poor and small countries that heavily rely on the income that the financial activities in the tax haven produce. To be able to redirect their production of income to other areas they will need support.

TAX COMPETITION AND EXEMPTIONS

On top of the revenue lost through the factors mentioned above, the use of tax incentives to compete for investments has been a cornerstone of development plans for many years. This is not illegal and is not included in the estimations of illicit capital flight discussed in this report, but since it means another huge loss of tax revenue for developing countries it is worth mentioning. Because taxed enterprises can enter into economic relationships with exempt ones to shift their profits through transfer pricing, it is also related to illicit capital flight.

Tax holidays or exemptions for investors are becoming commonplace. There is a race to the bottom, in terms of environmental, social and economic conditions for foreign direct investments, in which low income countries compete with each other to attract investment. Africa's low income countries reduced their corporate tax rate from 44% in 1980 to 33% in 2005[36]. A recent IMF survey of sub-Saharan Africa shows a remarkable increase in tax incentives: in 1980 less than half of sub-Saharan countries offered tax holidays; by 2005, more than two thirds did[37]. According to the same report, Zambia, for example, lost US$63 million in forgone revenue from 2004-2006 because of reductions in mining royalty payments[38].

The World Bank and the IMF are often cited as the sources of pressure on countries to open up to foreign corporations. One example of this is the Wold Bank and PricewaterhouseCoopers' annual 'Doing Business' indicator, which since 2006 has included a ranking of countries according to an estimate of the total tax rate incurred by companies[39]. The practice of offering tax incentives, however, is now under attack as economically unviable. Research has shown that lost revenue exceeds the benefits of increased investment. IMF is also recognising this. In the 2001 publication 'Tax Policy for Developing Countries' the IMF says:

"Of all the forms of tax incentives, tax holidays (exemptions from paying tax for a certain period of time) are the most popular among developing countries. Though simple to administer, they have numerous shortcomings. First, by exempting profits irrespective of their amount, tax holidays seem to benefit an investor who expects high profits and would have made the investment even if this incentive were not offered. Second, tax holidays provide a strong incentive for tax avoidance, as taxed enterprises can enter into economic relationships with exempt ones to shift their profits through transfer pricing. Third, the duration of the tax holiday is prone to abuse and extension by investors through creative re-designation of existing investment as new investment (for example closing down and restarting the same project under a different name but under the same ownership). Fourth, time-bound tax holidays tend to attract short-run projects, which are typically not as beneficial to the economy as longer term ones. Fifth, the revenue cost of the tax holiday to the budget is seldom transparent."[40]

In addition the IMF concludes that foreign investors - the primary target of most tax incentives - base their decision to enter a country on a whole host of factors, of which tax incentives are frequently far from being the most important. A United Nations report in 2000 also concluded that it is generally recognised that investment incentives have only moderate importance in attracting FDI[41]. The revenue loss that tax-competition leads to can in the long term end in an investment loss rather than attracting FDI, as multinational companies prioritise the quality of infrastructure, a well-educated workforce and a dynamic local market far higher than tax advantages when investing in countries[42].

Because tax incentives are frequently targeting foreign investment, they can create unfair competition in sectors where both national and international companies compete, and harm domestic entrepreneurship and investment[43]. The visible concessions offered to foreign business could also encourage tax evasion and avoidance by domestic companies and individuals[44].

The lower average corporate tax revenues that tax competition leads to often result in a shift of the tax burden towards wages and consumption. This shifts the tax burden onto domestic taxpayers whose means are likely to be less, and most of whose spending would stay within the national economy. This harms employment generation and increases inequality, and ultimately could slow economic growth[45].

With all this in mind it should be said that carefully used tax incentives could also be deployed in a positive way for poor people, for example as part of an industrial development strategy. A part of the problem is that tax incentives are frequently negotiated outside the legislative framework. It is for example common practise in the extractive sector to include tax exemptions in large mining contracts, but these are not made available for public scrutiny. In many countries, parliaments have no oversight or opportunity to debate the tax incentives offered in mining contracts at all[46].

MEASURES BY EUROPE AND THE INTERNATIONAL COMMUNITY

By Kristina Fröberg

International measures to stop capital flight from developing countries would also benefit developed countries. Rich countries also lose huge amounts of tax revenue due to illicit capital flight. Sweden for example loses around SEK46 billion per year in tax revenue due to illicit transactions related to tax havens[47]. This is almost 6% of the total tax revenue in the Swedish state budget of 2009[48], and one and a half times what is spent on aid.[49] In the UK the difference between the corporate tax that should have been paid according to tax liability and what is actually paid was somewhere between 9% and 33% in 2005.[50]

Although rich countries have much better margins than poor and middle income countries, and suffer less from illicit capital flight, the money lost is still important to their budgets, especially during hard times like financial crises. To stem capital flight, rich countries have organised tax cooperation through the Organisation for Economic Cooperation and Development (OECD). Tax cooperation in the OECD has mainly been focused on exchange of information between states, so that bank secrecy in tax havens is opened up to tax authorities and illicit capital flight can be tracked and stopped. But the OECD model for tax information agreements has been designed to suit rich countries, and thus developing countries haven't yet been able to make use of them.

In the following chapter, measures to hinder capital flight that would bring about a win-win situation for both developing and developed countries are presented. Among them are a new form of information agreements that also would benefit rich countries more than the existing agreements, since they include more countries and cost less to negotiate and use. The other measures presented would provide completely new tools and possibilities for both poor and rich countries to track capital flight.

MEASURES ALREADY TAKEN BY EUROPE AND THE INTERNATIONAL COMMUNITY

Actions already taken by the G20 and OECD

The first time that governments of the major economies acknowledged the impact of international tax rules and illicit capital flight on developing countries was during the G20 Summit in London in April 2009. At the Summit a commitment to "developing proposals, by the end of 2009, to make it easier for developing countries to secure the benefits of a new cooperative tax environment" was undertaken.

G20 MAJOR ECONOMIES

The Group of Twenty Finance Ministers and Central Bank Governors (G20) is a group of finance ministers and central bank governors from 20 economies: 19 countries plus the European Union. Their heads of government or heads of state have also periodically conferred at summits since their initial meeting in 2008. Collectively, the G-20 economies comprise 85% of global gross national product, 80% of world trade (including EU intra-trade) and two-thirds of the world population. Its leaders announced on September 25, 2009, that the group will replace the G8 as the main economic council of wealthy nations.

The members are: Argentina, Australia, Brazil, Canada, China, France, the European Union, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, the United Kingdom, and the United States.[51]

These developments at the G20 Summit were in part the result of an unprecedented banking crisis with some of its roots in offshore finance - a global recession that meant governments desperately needed every last penny of revenue income. Other factors behind the developments were high-profile examples of tax evasion uncovered in Lichtenstein and Switzerland, a new US president with a track record of seeking to stop tax haven abuse, and nearly a decade‘s worth of campaigning and research by academics, activists and development organisations in civil society[52].

The centre of the current global political debate rests with two groups of the world's richer countries - the G20 and the Organisation for Economic Cooperation and Development (OECD)[53]. The G20 has taken the lead on pushing for stronger tax cooperation measures (which means information exchange between states so that illicit flows of money can be tracked), and sanctions on tax havens that do not comply. It has bolstered support for the OECD, which is the global body with the greatest technical expertise on tax cooperation. The OECD has a forum for tax administration, which operates a peer review mechanism through which countries' cooperation on tax matters is assessed.

The OECD black, grey and white list of tax havens

The most high profile outcome at the G20 Summit in April 2009 was the creation of a black, grey and white list of tax havens, assessed in terms of their level of tax cooperation. As a criteria the list uses the number of bilateral information exchange agreements that a state has signed with other states (one by one). These are based on standards developed by the OECD. The list is backed by several sanctions, and G20 leaders stated that "lack of transparency and failure to exchange tax information should be vigorously addressed"[54].

The black list contains jurisdictions that have not committed to the OECD tax standard for information exchange agreements. They are called uncooperative tax havens. The grey list is made of jurisdictions that have committed to the tax standard, but have not yet substantially implemented it. To be considered as having substantially implemented the tax standard, a jurisdiction has to have 12 bilateral information exchange agreements in place. When this is done the jurisdiction can qualify for the white list[55].

The threat of being blacklisted led to a series of diplomatic activities where tax havens committed to signing tax information exchange agreements (TIEAs) with other jurisdictions, often with other tax havens or states with small populations. As of October 27, 2010, there were no jurisdictions left on the black list, and only 9 states left on the grey list (Liberia, Montserrat, Nauru, Niue, Panama, Vanuatu, Costa Rica, Guatemala and Uruguay)[56]. Over 150 exchange agreements had been signed with tax havens. However, because tax havens managed to fulfil the criteria through making agreements with other tax havens that would not request information exchange, or jurisdictions with small populations, this did not lead to the information exchange that many had hoped for.

In addition, the fact that the OECD model agreements are bilateral (signed by only two states) makes them costly and time-consuming for poor countries to negotiate. This means that a country's ability to sign an agreement is based on its economic power. By October 27, 2010, Mexico and Argentina were the only two developing states that had signed tax information exchange agreements with tax havens[57].

Moreover, the tax authority in a country which has signed an agreement has no automatic right to the information it requests (e.g. if a citizen or company holds an account and how much money it is worth). To receive the information, it has to prove that it is 'foreseeably relevant' to its administrative or enforcement work (in other words, allege a crime), and provide a large amount of information that it may not have. This is even more costly and time consuming. Because of this, even well-funded and resource-rich tax authorities like in the US have made few requests. Switzerland, for example, was able to state that its agreement to commit to OECD information exchange standards was consistent with maintaining banking secrecy[58]. It is very unlikely that developing countries would be able to take advantage of such agreements.

MEASURES NEEDED TO HINDER ILLICIT CAPITAL FLIGHT

International measures that could hinder illicit capital flight from developing countries are mainly about increasing transparency so that the illicit outflows can be traced and stopped. But they are also about strengthening the authorities that are to discover and correct them. If the international community is going to be able to develop and implement measures that will benefit all, these must be developed and implemented by a global body where both developed and developing countries are represented. This section presents the most important measures promoted by development organisations and academics, and describes the reactions and actions taken on them by EU institutions and other international bodies like the OECD.

Automatic and multilateral information exchange

With scarce resources, authorities in developing countries need more information to track down and tackle cases of tax evasion by multinational companies, money from criminal activities, individual corruption, or other illicit capital leaving their states. As mentioned earlier, it is nearly impossible for developing country tax authorities to acquire this information, either because information exchange agreements with other jurisdictions do not exist, or because they are too difficult to use.

Non-governmental organisations (NGOs) working with development have long argued that the bilateral web of information agreements in the existing model is too costly for developing countries, and that the agreement has to be truly multilateral if developing countries are to benefit from it. Participation in the system must mean just one agreement that includes the exchange of information with all other participants, and exchange with every state, no matter how poor, and it must be empowered with the threat of collective sanctions. The agreement must be open to any democracy to sign, and global in scope.

NGOs generally also conclude that if developing countries are to benefit, they also need access to tax information automatically. This means that they wouldn't have to spend money and time making a request for the information and prove that it is 'foreseeably relevant'. Rather than applying for information on a case-by-case basis, states would have immediate access to the information electronically.

The EU Savings Taxation Directive

Tax authorities within the EU already exchange information about individuals' savings income on an *automatic* basis under the EU Savings Taxation Directive (EUSTD). This shows that it is technically viable to exchange information automatically on a multilateral basis. If the EUSTD would be extended to include all types of capital income (not only individuals' savings but also other legal persons' capital income such as foundations, trusts, insurance companies and corporations), and to other non-European countries, it would enable the identification of tax evasion and avoidance practices to developing countries[59]. With 42 member states, the EUSTD is the largest multilateral arrangement providing for a working system of automatic information exchange. The coverage of the EUSTD is already not limited to EU member states but extends to 15 other secrecy jurisdictions, such as the Cayman Islands and Switzerland. In addition, negotiations are underway with Norway to become a member state. Large amounts portfolio investments of developing country residents are kept on deposit in Europe. This provides a strong case for developing countries to also have the opportunity to participate in the information exchange.[60] However, if tax authorities in developing countries are to be able to participate in the development of an automatic information exchange system, it must also include demand-driven technical assistance.

The OECD Joint Convention on Mutual Administrative Assistance in Tax Matters

Since 1988 there has been a Joint Convention on Mutual Administrative Assistance in Tax Matters of the Council of Europe and the OECD, which includes *multilateral* information exchange upon request. After an initiative from the UK which was announced at an OECD meeting on February 28, 2010[61], the convention has been opened up for all interested countries through an additional protocol. However, as of May 27, 2010, only 15 countries in total had signed the convention, and Mexico was the only developing country.[62]

The convention allows the parties to the convention to implement automatic information exchange, but it does not require it. The countries that wish to implement automatic information exchange would need to enter into additional bilateral agreements with each other to make it work. The Tax Justice Network concludes that "the Convention appears to provide a useful framework for information exchange upon request, for simultaneous and cross-border tax examinations, for the protection of data confidentiality and for a number of other important areas. It does not, however, make the material progress in the direction of automatic information exchange. If and when major developed countries agreed within the framework of the amending protocol to offer participants automatic information exchange, the attractiveness of this convention as an alternative to the EUSTD would increase. So far however, the only existing multilateral system of Automatic Information Exchange is the EUSTD"[63].

Actions on automatic information exchange by the European Parliament

The EU Parliament has adopted a number of reports and resolutions concerning capital flight that promotes automatic and multilateral information exchange. The most important one is perhaps the Domenici report, a resolution which was adopted by the Parliament with an overwhelming majority (554 votes to 46, with 71 abstentions) in February 2010.

In order to put an end to bank secrecy, the European Parliament recommends an *automatic* and *multilateral* exchange of information that should take place in all circumstances and without exemptions. As a first step towards a *global* framework for automatic information exchange, the Parliament wants to apply it to all EU Member States and dependent territories. The Domenici report also states that the commitments made by the G20 are not enough to tackle tax evasion. Likewise, it points out that the OECD framework for combating tax havens is unsatisfactory since it takes place only upon request. The Parliament calls on the OECD for the improvement of its standards, with the aim of making automatic and multilateral exchange of information the global standard.

Furthermore, the report calls for the expansion of the scope of the European Savings Tax Directive mentioned above to cover not only individuals, but also legal entities such as private companies (in particular multinational corporations) and trusts, as well as various sources of investment income. The European Parliament also calls for an extension of the provisions of the Savings Tax Directive to jurisdictions harbouring illicit capital flows such as Singapore, Hong Kong, Macao, Dubai, New Zealand, Ghana and certain states of the US.

The Domenici report strongly condemns the role played by tax havens, tax evasion and tax avoidance in hindering the achievement of the Millennium Development Goals and urges the Member States to make the fight against these activities a priority, while advocating the imposition of a regime of incentives and sanctions against illicit capital flights. For example, the following sanctions are considered: a special levy on movements to or from non-cooperative jurisdictions, non-recognition within the EU of the legal status of companies set up in non-cooperative jurisdictions, and a prohibition on EU financial institutions establishing or maintaining subsidiaries and branches in non-cooperative jurisdictions.[64]

EU communication on tax and development

In its Spring Package 2010, the EU Commission put forward a communication on tax and development: 'Cooperating with developing countries on promoting good governance on tax matters'. This put the issue high on the EU agenda for the very first time. European development organisations generally conclude that while the communication contains a good analysis of the problems related to illicit flows, there is a clear lack of concrete and ambitious proposals to solve these problems. It favours global conventions with binding commitments on transparency and exchange of information, and it supports the adoption and implementation of international standards, including through multilateral agreements and automatic information exchange. But as a concrete step forward it only recommends sharing experiences in international tax cooperation gained through instruments such as the EU Savings Directive, in order to explore the feasibility of multilateral agreements and automatic exchange of information[65]. The document constitutes a necessary but insufficient step in the right direction. On June 14, 2010, the EU Foreign Affairs Council passed a Conclusion that largely supported the Commission communication.[66]

FIGHTING ILLICIT CAPITAL FLIGHT THROUGH INFORMATION EXCHANGE

(between jurisdictions to be able to track tax evasion and avoidance, criminal activities and corruption)

Main actors	*Initiative*
Non-Governmental Organisations (Eurodad, Tax Justice Network, Christian Aid, Action Aid, Forum Syd, etc.) **European Parliament** (EU Commission and Council will share experiences to investigate further)	***Global automatic* and *multilateral* information exchange** where all countries can participate in one common agreement and make use of information exchange automatically regardless of the country's economic strength
EU through the **European Savings Tax Directive (EUSTD)**	***Multilateral* and *automatic* information exchange**. However, it only addresses individuals' savings income (not corporations etc.) and only includes EU member states + 15 tax havens
OECD through the **Joint Convention on Mutual Administrative Assistance in Tax Matters** (only 15 states participating by 2010)	***Multilateral* information exchange** where all countries can participate in the same agreement, but some might not be able to afford to make the requests needed to get information exchanged.
G20 and **OECD**	**Bilateral information exchange agreements**. Information exchanged between two states upon request if proven 'forseeably relevant'.

Country by country reporting

As mentioned earlier, almost two thirds of the illicit capital flight from developing countries originates from commercial transactions within multinational companies, through methods like transfer mispricing and falsified invoicing. This is hard to detect because international financial reporting standards (IFRS) only require multinational groups of companies to report on a consolidated basis. They must only present one set of accounts showing the overall financial activities and results for the group, without breaking them down for each country. Data for individual companies and countries is therefore aggregated, hiding all intra-group transactions.

If multinational companies were required to break down their financial results for each country of operation, it would enable tax authorities, media and civil society to see how much profit is made in each country, and how much tax should be paid. This is called country-by-country reporting[67]. Non-governmental organisations (NGOs) working to stop illicit capital flight from developing countries assert that it would be an important tool to uncover potential cases of tax avoidance and evasion. Country-by-country reporting should according to NGOs include a list of subsidiaries together with the turnover, profits, and taxes paid in each country, as well as the number and costs of employees, the nature and value of any assets owned, and information to show the extent of intra-group transactions[68]. A compulsory country-by-country reporting system adopted at a global level would dramatically improve the transparency of the activities and profits of transnational companies, and thus detect capital flight driven by tax evasion and avoidance schemes.

More than 100 governments worldwide, including EU member states, tend to incorporate international financial reporting standards into law. These are developed by the International Accounting Standards Board (IASB). The IASB is a private sector body which defines its stakeholders as shareholders and providers of capital. During the past years, civil society organisations have urged their governments, the EU, G20 and OECD to put pressure on the IASB to adopt a new standard that includes country-by-country reporting. If this happened, the majority of multinational companies would have to report their financial activities in every country where they operate.

Actions taken by the OECD

In July 2009, the UK Prime Minister Gordon Brown and the French President Nicolas Sarkozy called on the OECD to look at country-by-country reporting and the benefits of this for tax transparency and reducing tax avoidance[69]. In January 2010, OECD countries agreed that country-by-country reporting standards for multinational companies should be incorporated in the OECD guidelines for multinational companies by the end of 2010. But the guidelines are only guidelines, and are not binding. It is still up to each company to apply them or not. The OECD is currently also carrying out a technical feasibility study of a country-by-country reporting standard.

Actions taken by the EU parliament

In the previously mentioned Domenici report, a resolution which was adopted by the EU Parliament in February 2010, the Parliament recommends country-by-country reporting to become obligatory for transnational companies in the EU. The report also stresses that international accounting standards should be revised so as to establish a country-by-country reporting of companies' annual accounts. Furthermore, it suggests an "EU public register listing the names of individuals and undertakings having set up companies and accounts in tax havens, with a view to unveiling the true beneficiaries shielded by offshore companies"[70]. In a resolution from June 2010, the Parliament again calls for the enhancement of tax transparency by improving international accounting standards, adopting a country by country standard, and "systematic disclosure of profits made and taxes paid" by firms operating in developing countries[71].

Actions taken by the EU Commission and Council

The communication 'Cooperating with developing countries on promoting good governance on tax matters', published by the EU Commission in April 2010 and later approved by the EU Council Conclusions, calls for further investigation into country-by-country reporting. The Commission "supports ongoing research on a country-by-country reporting requirement of a reporting standard for multinational corporations, notably in the extractive industry". But no concrete commitments are announced to be taken by the EU in this respect in order to push a binding mechanism further[72]. Responding to the calls from the Parliament, the commission has committed itself to release a new communication on the issue by September 2011.

Actions taken by the International Accounting Standards Board and the World Bank

The International Accounting Standards Board (IASB, described on page 33) has responded to calls for greater transparency in financial accounting by consulting on an international accounting standard on country-by-country reporting for the mining industries. On the IASB website, many development organisations have contributed to a discussion paper on extractive industries, arguing for country-by-country reporting. The World Bank also has made a contribution to the paper which strongly supports a country-by-country reporting standard in the extractive sector.

The World Bank supports civil society arguments, stating that the IASB is far too concentrated on investors' opinions and does not pay enough attention to the public interest, which it should do according to its constitution. The World Bank also requests the inclusion of all the disclosure proposals on a country-by-country basis that the civil society coalition Publish What You Pay[73] proposes in an International Financial Reporting Standard, and argues that this is justifiable on cost/benefit grounds. The World Bank argues that the cost of introducing a country-by-country reporting requirement would not be too high because multinational companies are expected to already have data on a national basis for taxation purposes. Moreover, it points out that audited accounting information improves reliability and enhances the ability of shareholders to monitor the activities of a company.

The World Bank even states that in a sector as highly instable as the extractive industries, it is only possible to pursue reliable comparability analysis and gather comprehensive information to access financial, political, and reputational risks if these disclosure requirements are established. To counter the argument that a country-by-country reporting requirement would lead to a loss of competitive advantage by companies that apply it, the Bank argues that more than 100 countries require, permit, or are seeking convergence with International Financial Reporting Standards, and that mandatory country-by-country reporting will level the playing field better than voluntary regimes. Lastly, the World Bank states that more transparency will benefit capital providers[74].

The initiative by the World Bank to support country-by-country reporting is very welcomed by non-governmental development organisations, but they are also asking the World Bank to apply the reporting to its own activities. The International Finance Corporation (IFC), which is a member of the World Bank Group, supports private sector investment in developing countries.

Research has shown that a number of private sector beneficiaries of IFC funds use tax havens in their investments in developing countries. To ensure that this is not done for illicit tax purposes, the IFC should require all its beneficiaries to introduce country-by-country reporting[75]. Since the World Bank uses public money for the mission to "fight poverty with passion and professionalism for lasting results and to help people help themselves", it is especially important that it acts as a role model and combats illicit capital flight instead of contributing to it.

Actions taken by the United States

Since July 2010, country-by-country reporting is already mandatory for the extractive and energy companies registered in the US[76]. Oil, gas, and mining revenues are critically important economic sectors in about 60 developing countries, which, despite abundant natural resources, rank among the lowest in the world in poverty, economic growth, and governance assessments. The bill that was passed in July represents an important step in the right direction for many civil society organisations that have been advocating for such a standard.

FIGHTING ILLICIT CAPITAL FLIGHT THROUGH COUNTRY-BY-COUNTRY REPORTING

(requiring profit and tax paid to be reported by multinational companies in every country of production so that illicit capital flight can be detected)

Main actors	*Initiative*
Non-Governmental Organisations (Eurodad, Tax Justice Network, Christian Aid, Action Aid, Forum Syd, etc.) **European Parliament** (EU Commission and Council supports further investigations)	***Mandatory*** **country-by-country reporting for** ***all types of multinational companies***, starting with EU countries and incorporated in International Financial Reporting Standards by the International Accountants Standards Board
OECD through their guidelines for multinational companies	***Voluntarily*** **country-by-country reporting for** ***all types of multinational companies***
The World Bank recommends the International Accountant Standards Board to implement this in the International Financial Reporting Standards but does not apply it to their own beneficiaries. IASB is investigating this. Already mandatory for extractive industries registered in the **USA**.	**Country-by-country reporting** ***mandatory for the extractive sector***

A political mandate for the UN committee on tax matters

Combating illicit capital flight in a way that benefits developing countries requires a forum that can create and enforce global rules designed to benefit all. Today there is no global body with the political mandate, legitimacy, and technical expertise that is needed to do this.

The G20 and OECD, where work is proceeding fastest, are mainly 'rich countries' clubs, and are not representative of the majority of developing countries. Several middle income countries participate in the G20, but there is no regular low income country participation. While the OECD Global Forum is expanding to include some developing country representation, it remains a part of the OECD structure with membership dominated by rich countries and tax havens. It doesn't have the necessary legitimacy to handle political aspects of tax cooperation.

Capital flight and tax cooperation should ultimately be tackled by a representative political body with a political mandate from all countries. The United Nations' Economic and Social Council (ECOSOC) has an expert committee on tax matters. But this has only a technical mandate and not a political one. Lack of resources also limits both developing country participation and the secretariat of the committee.

The UN summits on 'Financing for Development' in Doha in 2008 and in New York in 2009 called on ECOSOC to "examine the strengthening of institutional arrangements to promote international cooperation in tax matters"[77]. In the negotiations before the summit in Doha, the G77 group of developing countries requested that the committee be upgraded to an intergovernmental body with a political mandate, but this did not make it into the final Doha communiqué.

Civil society organisations that work with capital flight promote as a first step that all governments should support the United Nations Committee of Experts on Tax Matters by strengthening it and upgrading it to an intergovernmental body. One major outcome of this should be a UN Code of Conduct on International Cooperation in Combating Tax Evasion, which is to be implemented at the national and international level.[78]

Strengthening tax authorities and repatriation

To meet their international poverty reduction commitments, developing countries must invest time, money and political will in strengthening national tax inspectorates to increase the domestic tax revenue collected and the size of their national budgets. For this to happen, rich countries and international donors must increase the funding for developing countries to strengthen their tax systems, surveillance, and collection, and to track illicit flows of capital. This should include making technical assistance available to developing countries that request it, for them to purchase from a service provider of their choice.

At the African tax inspectors meeting in South Africa in 2008, it was stated that: "Improving revenue performance will require a major improvement in tax administration through better service delivery, and taxpayer education, effective use of automated systems, better cooperation between tax administrations to counter tax evasion and aggressive tax planning, and strengthening audit and human resource management capability"[79]. As shown by examples on page 19, significant investment of resources, expertise and political will can substantially improve compliance.

Donors should make specific efforts aiming at recovering and repatriating stolen assets to developing countries. While some important steps are being taken by The World Bank and UN regarding corruption, the focus is biased by looking exclusively into the demand side of corruption while ignoring the supply side. This aspect of corruption needs to be tackled by shedding light on capital flight facilitators and tax havens.

For example, in 2007 the World Bank launched the Stolen Assets Recovery Initiative (StAR). This is an important step in tackling illicit capital flight. But since the StAR does not consider that there should be shared responsibility from banks and financial centres that host stolen assets, there is still much to be done. StAR also limits its role to a technical one, and is not promoting any regulatory measures whatsoever in order to tackle capital flight. Furthermore, by exclusively focusing on corruption-related flows, the bank is ignoring the biggest part of the picture represented by commercial flows, namely through tax evasion and avoidance schemes used by multinational corporations.

EXISTING INITIATIVES TO SHARE KNOWLEDGE

At the global level, initiatives to share knowledge already exist, such as the OECD's Global Relations programme, International Tax Dialogue, and the International Tax Compact (initiated by the German government). At the regional level, there is, for example, the African Tax Administration Forum. These are in need of encouragement and support.

NON-GOVERNMENTAL ACTORS IN EUROPE

There are a number of non-governmental organisations (NGOs) in Europe that work to stop illicit capital flight from developing countries. One of the first to do so and with the widest network around Europe is the *Tax Justice Network (TJN)*, which is an independent organisation launched in the British Houses of Parliament in March 2003. It is dedicated to high-level research, analysis and advocacy in the field of tax and regulation and work to map, analyse and explain the role of taxation and the harmful impacts of tax evasion, tax avoidance, tax competition and tax havens. TJN is not aligned to any political party, and its network includes academics, accountants, development organisations, economists, faith groups, financial professionals, journalists, lawyers, public-interest groups, and trade unions.

In particular, TJN aims to promote more local campaigns for tax justice, especially in developing countries, and to provide a medium through which tax justice issues can be promoted within multilateral agencies. For example, Richard Murphy, The founder of TJN, invented the idea of country-by-country reporting, now used by the OECD, EU and World Bank. Read more about TJN work and campaigns at *www.taxjustice.net*.

During 2007, *EURODAD* (European Network on Debt and Development) started their work on capital flight from developing countries. Eurodad is a network of 58 NGOs from 19 European countries working on issues related to debt, development finance and poverty reduction. Members like Christian Aid UK and Action Aid UK have been particularly active in working with capital flight from developing countries, both when it comes to research and campaigns. Southern networks that Eurodad works very closely with include Jubilee South, Afrodad, Latindadd and Third World Network. Read more about Eurodad at *www.eurodad.org*.

Despite the fact that resources lost through illicit capital flight far outnumber aid to developing countries or debt repayments from developing countries, the issue is not yet on the mainstream agenda of the majority of development NGOs or decision makers in Europe. If illicit capital flight from developing countries is to be stopped, wider knowledge and commitment among both NGOs and decision makers is needed.

ILLICIT CAPITAL FLIGHT FROM AFRICA

By Dr Attiya Waris

MAGNITUDE

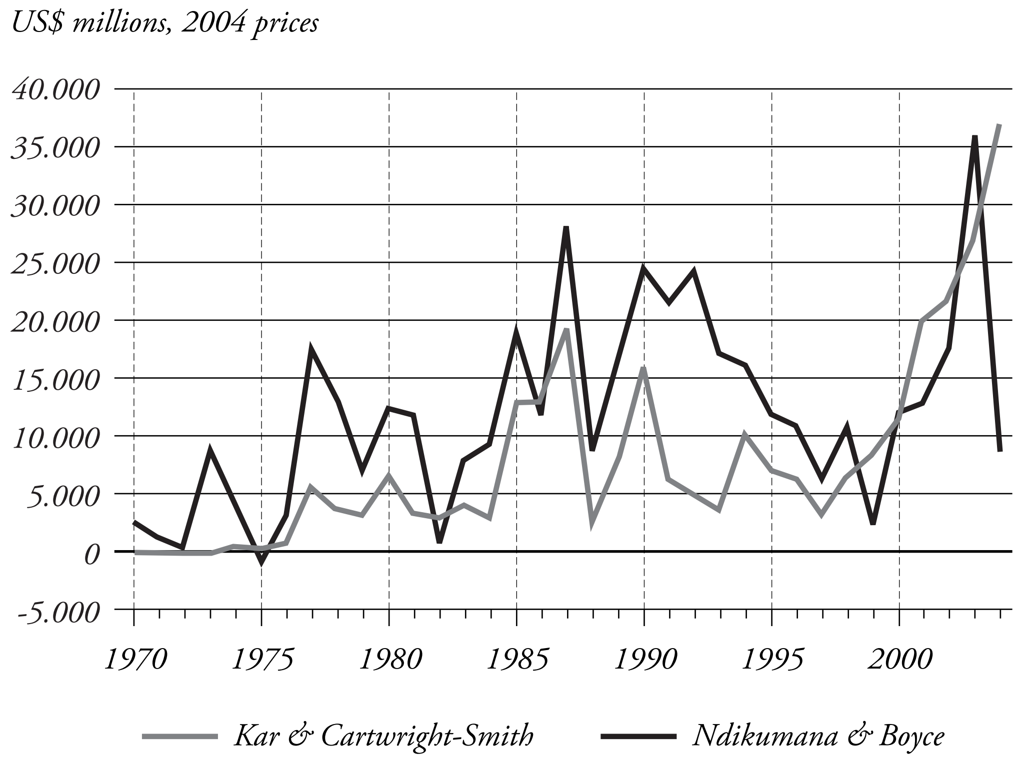
According to a report from Global Financial Integrity[80] (GFI) by Kar and Cartwright-Smith, Africa as a whole lost US$854 billion in cumulative capital flight over the period from 1970-2008. This is enough not only to wipe out the region's total external debt of around US$250 billion (at end 2008), but potentially to also leave US$600 billion for economic growth and poverty alleviation. The illicit flows grew at an average rate of 11.9% per annum in real terms over the 39 year period. It increased from about US$57 billion in the 1970s to US$437 billion over the nine years from 2000-2008.

Still, these estimates only address one form of trade mispricing, and do not include the mispricing of services, nor encompass the proceeds of smuggling, trade in narcotics and contraband, violations of intellectual property rights, human trafficking, or other illegal activities. Estimations of illicit capital flight from Africa also present the most analytical difficulties because countries with inadequate data account for almost 37% of regional GDP. Hence, Kar and Cartwright-Smith attempted to adjust for some of the factors responsible for the underestimation (by taking into account some of the components not covered) while clearly recognizing the limitations of such approximations. As a result of these adjustments, total illicit flows from Africa more than doubled from US$854 billion to 1.8 trillion[81]. However, estimations to adjust illicit flows generated through illegal activities were not included.

Another estimation by Boyce and Ndikumana[82] of the accumulated capital flight from just Sub-Saharan countries, and only between 1970-2004, calculates it to US$420 billion (converted to 2004 prices). With calculated interest[83] accumulation, capital flight is assumed to total over US$600 billion over the period. GFI has made more conservative estimations for Sub-Saharan Africa over the same period. A country was omitted from the total if it was deemed that their data were unreliable or if some of the data were incomplete[84].They found that Sub-Saharan Africa lost US$282 billion in capital flight in real 2004 dollars. But extending the period to 2008 sharply increased the cumulative total to US$533 billion, which shows a remarkable increase in capital flight from Sub-Saharan Africa over the last four years.

Some of the sharp acceleration in illicit outflows during 2000-2008 relative to earlier decades was undoubtedly driven by oil price increases, as well as increased opportunities to misprice trade that typically accompany increasing trading volumes due to globalization. Sub-Saharan Africa as a whole experienced the highest GDP growth rates in over 30 years during the period 2000-2008, underpinned by high commodity prices and structural reforms in a number of countries. Several researchers have pointed out that economic growth without credible reform could lead to more, not less capital flight, since the increase in incomes would simply finance the increased accumulation of foreign assets.

REAL ILLICIT FLOWS FROM SUB-SAHARAN AFRICA, 1970 - 2004



Source: Kar and Cartwright-Smith, (2010) Illicit financial flows from Africa: Hidden Resource for Development, Global Financial Integrity.

Studies of private wealth of High Net Worth Individuals (HNWI)[85] estimate that private wealth held in tax havens by Sub-Saharan Africans may constitute up to US$270 billion. The World Wealth Report 2008 estimated that there are about 101,000 Africans in this category, growing at an annual pace of 10%. Of these, 2% are considered as Ultra-HNWI[86], amounting to only 2170 persons on the entire African continent (the total population is around 1 billion). However, this figure may be an inaccurate estimate at best, as assets of wealthy and especially ultra-wealthy Africans are likely to be spread to various family members, while also trust or incorporated accounts are not identifiable to a single person.

Research at Global Financial Integrity on the absorption of illicit funds shows that while some of the private assets held outside their countries by developing country nationals might be legitimate, the bulk of such funds are certainly not[87].

Regional and country outflows

Despite the difference in samples and data between the estimations of GFI and Boyce and Ndikuma, 15 of the top 20 countries with cumulative illicit outflows are identified by both studies. They are Angola, Cameroon, Republic of Congo, Côte d'Ivoire, Ethiopia, Gabon, Ghana, Madagascar, Mozambique, Nigeria, South Africa, Sudan, Tanzania, Zambia, and Zimbabwe.

While an overwhelming part of illicit outflows from Africa has been from Sub-Saharan countries, there are significant disparities in the regional pattern of illicit flows. For example, outflows from West and Central African states, which by far are the biggest from the Sub-Saharan region, is mainly so because of the high outflows from Nigeria, which also is included in the economic group 'fuel exporters'. The proportion of illicit flows from West and Central Africa might be also be somewhat overstated because other regions in Africa include many countries that are poor reporters of data and thereby understate their contributions to illicit flows. Flows from the Horn of Africa and the Great Lakes region are also likely to be understated because of lack of data from Eritrea, Somalia and Sudan, as well as DR Congo, Rwanda and Uganda. Hence, the long-term evolution of illicit flows from different regions of Africa needs to be interpreted with caution.

Millions of US Dollars

Total illicit financial flows

	1970s	1980s	1990s	2000-2008	1970-2008
Africa	**57,291**	**203,859**	**155,740**	**437,171**	**854,061**
North Africa	19,161	72,020	59,813	78,742	229,737
Sub-Saharan	38,130	131,839	95,927	358,429	624,324
Horn of Africa	2,354	14,131	5,108	15,603	37,197
Great Lakes	6,925	16,079	4,978	10,285	38,267
Southern	5,894	20,581	31,447	116,828	174,751
West and Central	22,956	81,047	54,394	215,712	374,109
Fuel-exporters	20,105	67,685	48,157	218,970	354,917
Nonfuel-exporters	7,867	26,517	22,375	23,342	80,102

Average illicit financial flows

	1970s	1980s	1990s	2000-2008	1970-2008
Africa	**7,299**	**21,678**	**17,813**	**50,328**	**29,021**
North Africa	3,097	7,754	6,316	9,166	6,866
Sub-Saharan	4,202	13,924	11,497	41,162	22,156
Horn of Africa	249	1,421	715	1,949	1,183
Great Lakes	745	1,778	580	1,286	1,142
Southern	811	2,412	4,659	13,388	9,635
West and Central	2,397	8,313	5,544	24,538	10,196
Fuel-exporters	2,239	6,922	5,105	24,806	9,878
Nonfuel-exporters	1,017	2,729	2,433	2,787	2,502

Rates of change (real 2008 CPI deflated)

	1970s	1980s	1990s	2000-2008	1970-2008
Africa	**18,9**	**-2,1**	**-4,8**	**24,6**	**12,1**
North Africa	14,0	-11,5	0,5	6,0	6,5
Sub-Saharan	n.a.	1,3	-7,0	30,1	15,1
Horn of Africa	n.a.	7,3	-15,5	33,5	20,0
Great Lakes	13,2	-12,7	-17,7	35,0	13,5
Southern	n.a.	13,5	7,3	21,5	16,7
West and Central	21,5	0,0	-11,4	36,0	14,5
Fuel-exporters	n.a.	2,2	-15,6	42,6	21,8
Nonfuel-exporters	n.a.	11,3	-1,6	11,0	13,6

Source: Kar and Cartwright-Smith, (2010) Illicit financial flows from Africa: Hidden Resource for Development, Global Financial Integrity

Boyce and Ndikumana estimate capital flight and break it down for a sample of African countries in the table on page 43. The table summarizes the magnitude of capital flight from the sample of 40 sub-Saharan African countries.

Total capital flight (in US$ million 2004 and % of GDP), stock of accumulated capital flight which includes imputed interest earnings (US$ million and % of debt stock) over 1970-2004 period[88]

	Real CF	Stock of CF in 2004	Total CF/GDP (%)	Stock of CF/Debt (%)
Angola	42178.8	5095.6	215.6	5535.2
Benin	-3989.7	-7663.9	-98.6	-399.9
Botswana	1127.9	-1086.9	12.6	-207.4
Burkina Faso	3076.9	4670.6	73.6	269.0
Burundi	2073.6	2566.6	312.2	185.3
Cameroon	18378.9	27287.7	116.5	287.4
Cape Verde	2190.9	2707.1	231.1	523.6
Central African Republic	1943.8	2774.1	148.7	257.4
Chad	1337.7	2345.6	31.1	137.9
Comoros	-176.3	-168.7	-47.8	-55.2
Congo, Dem. Rep.	19572.5	36737.6	295.1	310.3
Congo, Rep.	14950.4	17474.8	344.3	299.8
Cote d'Ivoire	34349.4	54000.6	222.0	460.0
Ethiopia	17031.5	22526.0	175.0	342.6
Gabon	8580.8	11997.6	118.7	289.1
Ghana	8503.7	11208.4	98.7	159.3
Guinea	551.2	1048.9	14.6	29.6
Kenya	2665.4	6369.3	16.6	93.3
Lesotho	407.4	893.4	29.8	117.0
Madagascar	7430.9	9570.8	170.3	276.4
Malawi	2527.8	3825.4	132.9	111.9
Mali	-372.0	-425.4	-7.6	-12.8
Mauritania	2319.1	4008.0	151.2	174.4
Mauritius	-962.8	650.1	-16.0	28.3
Mozambique	10677.7	14273.4	180.6	306.9
Niger	-5975.7	-8732.6	-195.7	-447.8
Nigeria	165696.7	240781.0	230.0	670.9
Rwanda	3366.8	5889.5	183.5	355.7
Sao Tome and Principe	723.3	1059.1	1265.9	292.4
Senegal	-8885.0	-13077.3	-114.3	-332.0
Seychelles	2700.9	2986.3	384.1	485.7
Sierra Leone	4607.7	7005.4	424.7	408.6
South Africa	18266.0	17492.3	8.5	176.0
Sudan	9218.7	16325.0	43.0	84.4
Swaziland	1263.9	1342.6	50.2	285.6
Tanzania	5185.2	9963.4	45.8	127.7
Togo	-3481.6	-4064.6	-168.9	-224.3
Uganda	4982.0	6853.7	73.0	142.1
Zambia	9769.5	19814.3	180.2	272.2
Zimbabwe	16162.0	24556.0	344.2	511.9
Total	419975.7	606733.7	81.8	291.3

Notes: for Burkina Faso, the last year where CF is available is 2003; therefore totals, stocks, and ratios refer to 2003.

Source: Ndikumana L and Boyce JK (2008) New estimates of capital flight from sub-Saharan African countries: Linkages with external borrowing and policy options, Political Economy Research Institute, University of Massachusetts Amherst

EFFECTS ON DEVELOPMENT

Capital flight from African countries represents a higher burden, as a percentage of GDP, than in other developing regions[89]. Researchers and economists argue that Africa's staggering loss of capital through illicit outflows seriously hampers the continent's efforts at poverty alleviation and economic development[90]. The magnitude of the outflows explains why donor-driven efforts to spur economic development and reduce poverty have been underachieving in Africa.

Capital flight constitutes a diversion of scarce resources away from domestic investment and other productive activities. African economies have achieved significantly lower investment levels than other developing countries in recent decades[91]. The African continent is also the most capital-scarce among all developing regions. Estimates show that if Africa were able to attract back the flight component of private wealth, domestic capital stock would rise by about two thirds. Africa's GDP per capital is also estimated to be 16% lower than it would be if the continent had been able to retain its private wealth at home[92]. The leak of capital is likely to be accompanied by losses of human capital due to outward migration and to missed opportunities for 'learning-by-doing' amongst entrepreneurs and financial institutions[93].

Capital flight is also likely to increase inequalities of income in Africa. Individuals who engage in capital flight are generally members of economic and political elites, who take advantage of their privileged positions to acquire and channel funds abroad. Both the acquisition and the transfer of funds often involve legally questionable practices like the falsification of trade documents (trade misinvoicing), as well as the embezzlement of export revenues and kickbacks on public and private sector contracts. The shortages of revenue and foreign exchange resulting from this hit the less wealthy members of the society hardest. Finally, when national financial imbalances due to capital flight result in devaluation, the wealthy who hold external assets are shielded from the effects, while the poor have to take the consequences.[94] As long as illicit capital continues to flow out of poor African countries at a rapid pace, efforts to reduce poverty and boost economic growth will be undermined as income distribution becomes ever more skewed.

Governor Ndung'u of the Central bank of Kenya noted in a speech to Governors of African central banks that: "In the short run, massive capital outflows and drainage of national savings have undermined growth by stifling private capital formation. In the medium to long term, delayed investments in support of capital formation and expansion have caused the tax base to remain narrow. Naturally, and to the extent that capital flight may encourage external borrowing, debt service payments also increased and further compromised public investment prospects. Furthermore, capital flight has had adverse welfare and distributional consequences on the overwhelming majority of poor in numerous countries in that it heightened income inequality and jeopardized employment prospects. In the majority of countries in the sub-region, unemployment rates have remained exceedingly high in the absence of investment and industrial expansion"[95].

CAPITAL FLIGHT AND DEBT

It is generally expected that developing countries, facing scarcity of capital, will acquire external debt to supplement domestic saving. The rate at which they borrow abroad - the sustainable level of foreign borrowing - depends on the links among foreign and domestic saving, investment and economic growth. The main lesson of the standard 'growth with debt' literature is that a country should borrow abroad as long as the capital thus acquired produces a rate of return that is higher than the cost of foreign borrowing.[96]

Countries in Sub-Saharan Africa have generally adopted a development strategy that heavily relies on foreign financing from both official and private sources. Unfortunately, this has meant that for many countries in the region, the stock of external debt has built up over the decades to a level that is widely viewed as unsustainable.[97] Money originating outside Africa cannot be taxed, and it is the poor people in Africa that indirectly pay for the external debts. It has been argued that hindering capital flight could bring in much needed capital that would not only stimulate African economies but possibly replace the need for external debt.

According to estimations made by Ndikuma and Boyce, the group of Sub-Saharan African countries is a 'net creditor' to the rest of the world in the sense that their private assets held abroad (as measured by capital flight including interest earnings) exceed their total liabilities as measured by the stock of accumulated external debt. Their external assets (accumulated capital flight minus accumulated external debt) amounted to US$398 billion over the period 1970-2004. The accumulated capital flight is three times as high as the accumulated debt stock.

Foreign debt and capital flight have also been found to be closely interlinked. Research by economists and political scientists suggests that a large extent of the capital flight from Africa has been public loans that were channelled out of the country as private funds. A 'revolving door' relationship has been identified between debt and capital flight. In some cases, as much as 80 percent of the public loans have left the country as private assets through capital flight.[98]

Ndikumana and Boyce (2008) found that out of every dollar of new external borrowing, as much as 60 cents left the country in the form of capital flight the same year. Their results support the hypothesis that debt overhang has an independent effect on capital flight: a one-dollar increase in the stock of debt adds an estimated 3-4 cents to annual capital flight in subsequent years[99]. Collier, Hoeffler, and Pattillo (2003) report an almost identical result, with a one dollar increase in the stock of debt leading to 3.2 cents of capital flight.

Foreign borrowing can cause capital flight by contributing to an increased likelihood of a debt crisis, worsening macroeconomic conditions, and the deterioration of the investment climate. Foreign borrowing also provides the resources for channelling private capital abroad. But capital flight can also lead to more borrowing, since capital flight drains national foreign exchange resources, forcing governments to borrow abroad[100].

STAKEHOLDERS – THE AFRICAN CONTEXT

The groups of stakeholders engaging in capital flight or trying to stop it in Africa are the same as in the rest of the world. Global Financial Integrity estimates that approximately 60-65% of the illicit capital flight from developing countries stems from commercial transactions within multinationals, 30-35% from criminal activities like trades of weapons, drugs and humans, and 3% from corruption. While GFI have not attempted to verify these approximate percentages for Africa, they believe that these are likely to be of roughly the same order of magnitude[101]. This section explores the specific context that some of the stakeholders face in Africa.

States

African judiciaries, legislatures and executives generally have difficulties in understanding the diverse aspects of capital flight and how they are reflected in the domestic economy. Tax administrations generally suffer from large capacity constraints underpinned by lack of support from donors, making it difficult to assess and collect taxes. Other constraints include:

1. Lack of fiscal legitimacy. A general lack of trust on the part of citizens in the quality of public spending.

2. Shallow tax base. Governments are unable to bring informal actors — large and small — into the tax net. In particular, the existing tax base is eroded by the excessive granting of tax preferences and the inefficient taxation of extractive activities.

3. Unbalanced tax mix of African countries. Many countries rely excessively on a narrow set of taxes to generate revenues for their state and some stakeholders are disproportionally represented in the tax base.[102]

Procurement processes also add to the problem with capital flight. For example, Nigeria borrowed money from the World Bank to complete its multi-billion dollar steel complex. Some money disappeared. Some was squandered and mismanaged, causing the national debt to increase. When Nigeria repays the World Bank for a non-operational steel mill that payment will become capital flight. In other words, it is the flight of money capital caused by the lack of intellectual capital.

Secrecy jurisdictions in Africa

Within the African region, Mauritius and the Seychelles have been classified by some experts as financial tax havens. They are both regarded as particularly vulnerable or weak states. Mauritius' potential weakness stems from its offshore financial regime, which permits corporate institutions with no physical productive presence within Mauritius to open and operate bank accounts. From the standpoint of the offshore corporation, the rationale for establishing offshore is to take advantage of the lower rate of taxation in comparison to neighbouring jurisdictions. The primary incentive for the offshore jurisdiction is the revenue to be extracted through taxation and the potential to increase employment levels in the financial services sector. As a strategy to offset weaknesses in other areas of economic productivity, such as manufacturing and mining, offshore centres are likely to proliferate in the sub-region in the short to medium term. In 2001, Botswana took measures to diversify its tertiary services sector by establishing an international financial services companies (IFSCs) regime. Income tax legislation facilitates the establishment of an International Financial Services Centre to facilitate and regulate an offshore investment sector. The sector will benefit from a taxation rate of 15%, which is 10% lower than the prevailing average corporate rate.

An analysis of the offshore financial system in the sub-region indicates that one of its attractions is the relatively high level of confidentiality that it offers concerning the identity of shareholders of corporate entities operating in it. Although directors' and shareholders' names are filed with the government registry in Mauritius, the register is not accessible to the public. Mauritius has repeatedly expressed its commitment to maintain its status as a premier off-shore financial centre, and its acknowledgment of the vulnerability to tainted funds that this entails.[103]

In addition, other African countries are continuing to set up Exclusive Economic Zones as well as Trade Free Zones and Free Ports, all of which are the first and lowest level of a tax haven. The impact is manifold. There is a race to the bottom in an attempt to lure in investors using low taxes as a strategic fiscal policy. On the other hand, the state practicing this policy forces the hand of its neighbouring states to follow suit, while at the same time providing a bolt-hole for illicit money that can no longer be kept in banks in other tax havens that are falling under more and more scrutiny (especially the OECD member states whose banking institutions are utilising secrecy provisions). The existence of the African tax havens may not only allow for an increase in capital flight. The very nature of poor record keeping may allow even the most basic scrutiny where legitimate being rendered impossible.

Corrupt leaders and money laundering by criminals

There has been discussion on the impact that corrupt leaders and crime are having on capital flight.[104] Corruption is seen as a key part of illicit outflows.[105] No example expresses the African experience in capital flight as well as that of Mobutu Sese Seko.

> ***If capital flight could be personified, then the infamous Mobutu Sese Seko did. The kleptocratic ruler is said to have looted US$5 billion (World Bank Report, June 2007) and most of it is alleged to have been deposited in Swiss Bank Accounts.***

Money laundering takes the form of currency transactions, the illegal purchase and sale of minerals like diamonds, as well as the use of front companies and the round tripping of money, which involves sending money back and forth to clean it. Interpol has on occasion called upon the national commercial crime units to carry out money laundering enquiries on behalf of state law-enforcement authorities in Africa. This has entailed carrying out enquiries concerning banking transactions and property acquisitions by persons under investigation in countries which have anti-money laundering legislation. (Currently there are approximately 22 African countries with anti-money laundering legislation and 4 with none at all. The remainder have not been fully researched.[106])

In spite of the onerous legislative requirements and harsh criminal penalties imposed on diamond operators, diamonds are still stolen from the mining areas on land and sea. Illegal diamond and natural resource deals are also very difficult to detect because, like bribery and corruption, they are conducted in a very secretive manner by parties who all stand to benefit from non-compliance with the law. Therefore, in order to detect, interdict and prosecute offenders, the law-enforcement agencies have to rely on setting traps and mounting 'sting operations', which can be very dangerous, and have on a number of occasions led to the murder of law enforcement officials.

An extensive report by CCFD in French, entitled 'Ill-gotten goods, who benefits from the crime?', reviews the stolen assets of more than 30 leaders from developing countries, which amounts to more than US$100 billion. It reports that to date, rich countries have returned only 1-4% in stolen assets, this despite repeated promises to fight against corruption. The central issue of the report addresses why this is continuing to take place, and finds the answers in the existence of tax havens, lending to corrupt regimes, and plundering of wealth from natural resources.[107]

The Financial Action Task Force on Money Laundering (FATF) estimates the extent of global money laundering at two to five percent of world economic output. The interim findings of the ISS research project suggest a significantly large scale of money laundering in the Eastern and Southern Africa anti-money laundering group region. In addition, the United Nations Office on Drugs and Crime has begun work on anti-money laundering, using three East African countries (Rwanda, Tanzania and Uganda) as case studies.[108]

Civil society in Africa

African audiences will find it easier to understand "money capital" because it directly yields tangible products that they can touch, smell or hear. However, despite this, there is a lack of understanding by citizens, especially in grass root communities, that the amount of tax paid is actually a trust given to the state to help them. This leads to a similar lack of understanding that capital flight is a direct loss of money that could also be used to assist them. Currently, there are some limited civil society organisations beginning to work in the area of capital flight. However, they are beset by many problems. These include:

1. A lack of understanding of how the issue of capital flight links with their ongoing campaigns.

2. A lack of understanding in society of their right over tax collected and its need to be redistributed for their benefit.

3. Government understanding and analysis of financial issues is limited, in particular amongst parliamentarians, and hence oversight is poor

4. Strong private sector lobbying as well as a strong push by international institutions to privatise and fall in with the current international procedures has led to the status quo being maintained.

5. A lack of freedom of information in most African countries means that even if there was capacity there may be no access to data in order to analyse the situation on the ground.

As a result, the few non-governmental organisations in Africa that are working on the issue of capital flight come at it mainly from the vantage point of debt relief campaigns, taxpayer associations, as well as some human rights and development based institutions such as AFRODAD, CRADEC, ISODEC, and Policy Forum (See appendix page 68-73).

However, civil society organisations of different types are beginning to work on issues concerning tax. UNIFEM is developing a gender budgeting project, and LICOCO in the DRC is looking into tax from the point of corruption. Even Greenpeace has engaged in studies of the effects of environmental degradation due to capital flight.[109] Both local and international organisations are all beginning to delve into understanding the effect that tax or the loss of tax collection has on societies. They are all in need of training and capacity building as a first step, followed by assistance in conducting research from their particular perspectives.

CASE STUDIES

KENYA *By Dr Attiya Waris*

Country facts [110]	
Population, total	*39.8 million (2009)*
GDP per capita	*US$ 759 current (2009)*
Life [111] expectancy at birth, total	*54 years (2009)*
Child malnutrition	*17% of children under 5 (2008)*
Literacy	*87 % of population age 15+ (2008)*
Mobile cellular subscriptions per 100 people	*42 (2009)*
Internet users per 100 people	*8.7 (2009)*
Poverty Ratio	*46.6% (2009)*
Total debt outstanding and disbursed	*US$ 7.44 billion (2008)*
Net official development assistance	*US$ 1.36 billion (2008)*

The tax base and collection of tax in Kenya

Any country's revenue base is largely determined by the structure of its industries, the output produced, and the composition of employment that goes along with production. Similarly, changes in tax rates have had an impact on the tax revenue collected, as do trade blocs and potential harmonization of tax rates between countries in a regional block.

Kenya is known across Africa for being one of the most active states in terms of tax collection efforts, having made significant gains in the past decades to recover its lost revenue capacity. In 2009, a peak in tax revenue was registered. A previous peak year of revenue collection was in 1994. It is argued that this record of recent gains is a return to the peak levels reached in the mid-1990s, rather than an unprecedented record. This is seen as the case in particular as there have been changes in the structure of the tax system. From 1994 onwards, trade taxes reduced in importance, while value-added taxes (VAT) increased slightly. The most sensitive taxes, however, have been the corporate and personal income taxes, which often follow political cycles.

However, Kenya's domestic and international underground economy remains a significant area of revenue losses, much of which is neither quantified nor tackled up to date. The reason for this is that in order to collect taxes from the domestic underground economy, the government would have to enter in revenue bargaining relationships with constituencies such as the informal sector, which by its very nature remains unregistered and unorganised and with whom as a result, the government has not kept up a continuous political dialogue. In engaging with the international underground economy, Kenya must deal with its international relations with other states, as well as the current international fiscal and economic laws and policies and their impact on Kenyan tax revenue.

Capital flight from and to Kenya

Contrary to popular belief, classifications of both the domestic and international underground economy include a vast amount of perfectly legal activities as we can see below.

CLASSIFICATION OF UNDERGROUND ECONOMY ACTIVITIES

Activity status	*Monetary transactions*	*Non-monetary transactions*
Legal activities	- Tax avoidance - Unreported income - Wages, salaries and assets from unreported work - Under invoicing - Employee discounts - Fringe benefits	- Tax avoidance - Barter of legal goods and services - All do–it-yourself and other unpaid help
Illegal activities	- Tax evasion - Trade in stolen goods - Drug dealing and manufacturing - Gambling and racketeering - Prostitution - Money laundering - Counterfeiting - Smuggling - Fraud	- Tax evasion - Barter of drugs - Theft for own use - Production of drugs for own use - Child labour

Source: KIPPRA 2007

Capital flight as evidenced form the above table includes currently both criminal and non-criminal activities. This table uses two classifications, firstly, illegal and legal activities, and secondly, barter and monetary issues, where in terms of scale the legal and monetary components far outweigh the illegal components in most developing countries including Kenya.[112] But transferring money out of the country without reporting it is illegal. When capital gets transferred across the border without being reported this becomes illicit capital flight.

An IMF study in 2000 found that trade misinvoicing is a significant problem for Kenya[113]. How money laundering takes place in Kenya was discussed in a report by the Institute of Security Studies, where areas as diverse as cattle rustling and drug smuggling were analysed to show the extent of the problem of capital leaving Kenya.[114] However, Kenya also finds itself on the other side of the fence. A recent statement by the Central Bank of Kenya (CBK) disclosed that there was a large amount of unaccounted for liquidity in the economy, and the problem was ascribed to the possible influx of pirate money into the Kenyan economy.[115] As a result, there are no exact figures as to how big this problem is on a national scale. There have been estimates as to the amount of unreported money moved out of the country by Fofack and Ndikumana. In 2010, they calculated the accumulated capital flight to date from Kenya as amounting to US$6.369 billion[116]. This could be compared with the total external debt stock of Kenya, which amounted to US$7.44 billion in 2008, according to the World Bank.

However, in Kenya, like many developing states in Africa, the revenue equation isn't only about technical parameters in estimating the amount lost through capital flight. Critical elements to the entire picture on capital flight include the legislative provisions and their utilisation in facilitating illicit capital flight, as well as the enforcement of the provisions both through the policing and judicial infrastructure. It's also an issue of consent, which means that the more the citizens can realistically expect from the government, the higher their consent to surrender part of their income to the revenue authorities.

The legal background

On August 4, 2010, Kenya voted in by referendum a new constitution. This constitution will have a large impact on the manner on which capital flight will be dealt with. Specific pertinent provisions of the Constitution include the followings:

Article 34 protects the independence and freedom of print, electronic and all other types of media with the effect that whistle blowers are protected in matters of public interest, e.g., if there has been misappropriation of public funds or in the illicit outflow of capital. This will encourage transparency and act as a deterrent to corruption by public officials.

Article 71 requires that all agreements relating to natural resources are subject to ratification by parliament if it involves the grant of a right of concession by or on behalf of any person, including the national government, to another person for the exploitation of any natural resource of Kenya. There are several dimensions to this. First, that contracts will become public knowledge upon presentation in Parliament, and second, that there will be parliamentary oversight, limiting the possibility of capital flight as well as loss of income through poorly negotiated contracts.

Article 75 relates to the conduct of state officers and specifically prohibits any state officer from compromising any public or official interest in favour of a personal interest. Part 2 of the same article provides for the punishment of the offending officer by removal from office or in accordance with the disciplinary procedure for the relevant office.

Article 76 prevents the illicit outflow of any income to any foreign bank, including but not limited to tax havens. It also deters any state officer from acquiring wealth by illegally acquiring money from public coffers or incurring external debts for personal gain.

Article 201 sets out the principle and framework of public finance that will guide the fiscal process in Kenya, as including the promotion of openness, accountability and participation of citizens in financial matters.

All these provisions in the new Kenyan Constitution are new, as yet unexplored and untested. In a referendum that came into force on June 28, 2010, before the new Constitution, the legislators also passed a Proceeds of Crime and Anti-Money Laundering Act (AML), which means that there is a strong political will to end capital flight from Kenya. The AML Act is comprehensive in that it criminalizes the offence of money laundering, establishes a financial reporting centre, stipulates anti-money laundering obligations for reporting institutions, establishes an assets recovery agency including its powers and functions, and also establishes a criminal assets recovery fund. The Act also has extensive and elaborate procedures for both civil and criminal forfeiture and international assistance in investigations and proceedings. The enactment of this Act provides Kenya with the requisite legal and institutional framework to tackle the problem of money laundering in the country.

Some key highlights of the Act include:

- Money laundering being declared a criminal offence punishable by up to fourteen years imprisonment and a fine of up to US$5 million.
- Persons intending to convey monetary instruments in excess of US$10,000 or its equivalent in any currency to or from Kenya will be required to report the particulars of such conveyance to authorised personnel.
- Reporting institutions will be required to report suspicious transactions and cash transactions above US$10,000 or its equivalent in any currency to a Financial Reporting Centre. They will also be required to verify their customers' identity, establish and maintain customer records, as well as establish and maintain internal reporting procedures.

If the legislative and constitutional framework is already in place, what remains is to ensure that the policy makers and stakeholders are capable of acting as responsible watchdogs to the processes and procedures put in place. In addition, there also remains the constant maintenance of the political will, possibly through public pressure as well as civil society pressure, to ensure that capital flight is at a minimum reduced and controlled.

To stop illicit capital flows there is also a need for international information exchange that reveals illicit Kenyan wealth held offshore, as well as reports on what profits multinational companies make in Kenya that should be taxed in the country.

Measuring capital flight from Kenya

Various causes of capital flight have been put forward over the past few years. A number of economists have singled out portfolio diversification motives, political and macroeconomic instability (particularly conflicts and macroeconomic volatility), fiscal deficits, and expected devaluation of local currencies, as some of the root causes of capital flight. However, recent data show that capital flight has continued to grow unabated even in recent years when fiscal deficits and macroeconomic volatility have been regulated, suggesting that there may be other determining factors, particularly, corruption and poor governance.[117] The form of capital flight here includes not only individual corruption but also tax evasion by multinational companies, for example through transfer mispricing (see page 17-18) which, according to an IMF study from 2000, is a significant problem for Kenya.

According to a report from Global Financial Integrity (GFI), the average of illicit outflows per year from Kenya during 2002-2006 is estimated at US$ 686 million.[118] This could be compared with the Net Official Development Assistance received, which for year 2000 was US$509 million, and by 2005 had risen to US$ 752 billion. Another report from GFI estimates that the average tax revenue loss per year from 2002-2006, due to just one form of trade mispricing, was US$ 48.55 million.[119]

Capital flight and inequality[120]

Illicit capital flight is one of the most pressing concerns when attempting to raise both the tax effort and levels of tax compliance among the top income earners. Kenya has its own share of large taxpayers, many of whom are likely to avoid their responsibilities by placing both their wealth and property outside of Kenya, while still living and working in the country. This phenomenon is commonly known as capital flight, and it can be described as illicit in the case where capital that has been moved abroad is either of criminal origin, or has broken the law in the country of origin by being moved abroad without being reported and evading tax[121].

Regarding wage inequalities in Kenya, it is estimated that 90% of the population that are workers and peasants in urban and rural areas earn at most 15,000 Kshs (approx US$250) a month. The 9% of the population that constitute various levels of the emerging middle class earn at most 100,000 Kshs (US$1660) a month. The top 1% of the population, which can be considered as the economic, social and political elite, earn above 100,000 Kshs (US$1660) a month.

These wealth inequalities are both a cause and a consequence of a lack of tax justice. Firstly, if there was a well-administered progressive income tax in Kenya, income inequalities would be significantly reduced. Secondly, with better international tax cooperation Kenya would be able to tax capital gains and wealth held offshore. Currently, it is nearly impossible to find out about such banks and corporate accounts. The low level of corporate tax payment is inherently linked to the practice of trade mispricing.

Advocacy and research gaps

A large part of the Kenyan economy is informal. Record keeping in both the formal and informal sector is largely absent, and money laundering would be difficult to detect in such an environment. An aspect of this informality is the widespread use of cash to transact legitimate business, which makes it easy to introduce cash, earned from crime, into the financial system. Record keeping by public authorities is in considerable chaos and has effectively imposed secrecy in the conduct of business transactions, which the law never intended.

This review clearly shows that there is a need for more in-depth and detailed knowledge on how banks are involved in and facilitate capital flight both into and from Kenya at the national, regional as well as continental and international levels.

At the national level, there is a need to strengthen the understanding of both citizens and policy makers of the effects of capital flight on the individual Kenyan as well as the overall development needs of the state. In addition, there is a need to take the legislation a step further and pursue its effective and efficient enforcement. Whether the current framework of guidelines are sufficiently addressing the particular context of Kenyan economy, which is (a) largely cash based, (b) heavily reliant on a parallel, informal banking system, and (c) where informal value transfer methods are the norm, is yet to be seen. NGOs and the media may play an important role in informing civil society of tax evasion and corrupt actions by publishing knowledge that is made easily available for the public.

Conclusion

Kenya, like most African countries, has the potential to collect more much-needed revenue. Tax evasion seems to be greatest in the corporate sector. Attempts to improve tax compliance can only be successful if the taxation is perceived to be participatory, transparent and non-coercive. This means that policy space for formulation and implementation of tax policy must be opened up to include a wider society. Debate on taxation should be carried out in the open and include all sectors of society if taxation is to play its role as a governance tool in the strengthening of democratic structures.

Fiscal legislation to stop illicit capital flight has been implemented during 2010, but there is a need to strengthen tax authorities to ensure compliance. There is also a need for information exchange to receive information on unreported wealth held in tax havens, as well as information on the profits that multinational companies are making in Kenya to be able to detect mispricing practices.

REPUBLIC OF SOUTH AFRICA *By Dr Attiya Waris*

Country facts [122]	
Population, total	*49.3 millions (2009)*
GDP per capita	*US$ 5798 current (2009)*
Life expectancy at birth, total	*51.5 years (2009)*
Literacy	*88% of population age 15+ (2008)*
Mobile cellular subscriptions per 100 people	*92 (2009)*
Internet users per 100 people	*8.6 (2009)*
Total external debt stock	*US$ 41.943 billion (2008)*
Net official development assistance	*US$ 1.125 billion (2008)*

Today, South Africa is considered the economic motor of Africa.[123] Unlike many other African states there has been active research for many years on capital flight issues in the South African context. Since capital flight involves the movement of money across borders, Foreign Direct Investment (FDI) becomes critical, as it involves the authorised capital that is allowed to move in and out of a state for the purpose of facilitation of investment. There is consistent data on FDI flows to and from South Africa available from 1956 and onwards. FDI is a good indicator of the amount of possible capital flight as it reflects the ease of movement of capital. The easier it is to move the money, the easier to conduct capital flight. It is also well established that FDI played a crucial role in the earlier development of the South African economy, and that there has been capital flight. For example, Rustomjee has analysed capital flight from South Africa under apartheid rule.[124] The end of apartheid in South Africa in 1994 increased competition in Africa, and large transnational companies seeking a single production or headquarter centre in Anglophone Africa moved to South Africa, making it the largest and strongest competing economy in Africa.[125]

South Africa, unlike many African countries, is involved in the international movement of capital as both a receiver and a distributor. While there continues to be capital flight out of South Africa to other states including tax havens, the current legal framework allows for capital flight into the country as well. These legal provisions encourage investment which has resulted in the investment of capital illicitly and legally, especially from other African states into the South African economy.

The legal background of the South African tax system

The power to collect and distribute taxation in South Africa is set out in articles 213-230 of the current South African Constitution.[126] In addition, there is an extensive and varied list of legislation on taxation.[127] South Africa has a residence-based tax system, which means residents are - subject to certain exclusions - taxed on their worldwide income, irrespective of where their income was earned. Non-residents are, however, taxed on their income from a South African source.

Foreign taxes are credited against South African tax payable on foreign income. The majority of the state's income is derived from income tax (personal and company tax), although nearly a third of total revenue from national government taxes comes from indirect taxes, primarily VAT.

The South African Revenue Service (SARS) estimates the tax loss in the country to be up to R30 billion (45% of government revenue)[128], largely due to evasion and avoidance by rich individuals and companies.[129] At the same time, South Africa has been listed as a tax haven by the Tax Justice Network.[130] An increase of the foreign exchange allowance to 750,000 Rand (US$120,000) has opened the financial floodgates in two directions. As investors are potentially surveying the horizons, the South Africa-based multinational banks are preparing to act, or have already done so. SARS has estimated that South Africa could be losing 64 billion Rand (approximately US$10 billion) to tax havens annually. Pravin Gordhan, the SARS commissioner, said in November 2010 that the German government was sharing information it had received about secret bank accounts in Liechtenstein.[131]

Measuring capital flight from South Africa

Smit and Mocke (1991) estimated that the accumulated capital flight from South Africa during the period 1970 to 1988 amounted to between US$12-23 billion, depending on the measure used. They point out that these amounts are large by international standards, and that during the late 1970s capital flight from South Africa exceeded that from Argentina, Brazil, or the Philippines.[132] Referring to a case study of South Africa by Fedderke and Liu (2002), Boyce and Ndikumana confirm that both the change in political rights dispensation and an index of political instability are positively related to capital flight.[133] Indeed, the SSA countries with the most developed financial systems have relatively low levels of capital flight (for example Kenya, Mauritius, Seychelles).[134]

The accumulated capital flight from South Africa between 1970 and 2004 has been estimated by Boyce and Ndikumana as amounting to US$18.266 billion, however, the trade misinvoicing adjustment could not be calculated in the case of South Africa due to lack of consistent data.[135] In 2010, Global Financial Integrity (GFI) estimated that the accumulated capital flight from South Africa between 1970-2008 amounted to US$81.840 billion. During the period 2005-2008 alone, capital flight from South Africa was almost US$57 billion, which shows a significant increase in capital flight over the last few years[136]. In particular, there was a rise in 2007 and 2008. This could be compared with the total external debt stock of the country which in 2008 amounted to US$41.9 billion.

Another GFI report estimated the average capital flight from South Africa between 2002-2006 at US$ 6.445 billion per year.[137] According to the study 'The implied tax revenue loss from trade mispricing' (also by GFI), the yearly average of capital flight due to just one form of trade mispricing from SA was US$3.872 billion for the same period, and the yearly average tax revenue loss was US$ 1.084 billion[138]. This means that just one form of trade mispricing by multinationals constituted more than 60% of total capital flight during 2002-2006. The revenue loss from this could be compared to the Net Official Development Assistance which in 2000 was US$486 million and in 2005 had risen to US$690 million, approximately half of what was lost in revenue due to one form of trade mispricing.

During the last 13 years of apartheid, from 1980 to 1993, average capital flight as a percentage of GDP was 5.4 percent a year. Post-apartheid, from 1994 to 2000, capital flight rose to an average of 9.2 percent of GDP per year.[139]

Gross Fixed Capital Formation (GFCF) is a measure of the net new investment in capital goods (fixed capital assets) by enterprises in the domestic economy during an accounting period. Fixed capital investments typically increase productivity and GDP growth. During 1980-1985, capital outflows as a percentage of GFCF in Africa averaged 39 percent, dropping to 9 percent from 1986-1993. During 1994-2000, capital flight as a percentage of GFCF averaged a high of 58 percent. On the whole, it is clear that a very large amount of investment has been foregone in South Africa as a result of the magnitude of capital flight.[140]

South African Revenue Service and the South African Government, in recognition of the peculiar problems facing the confidence of investors, have given tax amnesties for capital flight. Once in 2003, and now again in October 2010, the discussion on another amnesty is back on the table.[141]

Capital flight and inequality

As discussed earlier in chapters 1 and 3 (page 14 and 44), inequalities in income are increased and the gap between rich and poor is widened by capital flight.

The economy of South Africa is two-tiered: one rivaling other developed countries, and the other with only the most basic infrastructure. It is therefore a productive and industrialised economy which at the same time exhibits many characteristics associated with developing countries, including a division of labour between formal and informal sectors and an uneven distribution of wealth and income. The primary sector, based on manufacturing, services, mining, and agriculture, is well-developed. UN Habitat figures show that South Africa's urban population is now at 58 percent, and of the total urban population, 33 percent are living in slums and squatter camps where basic service delivery is poor.[142]

Overall distribution of wealth is still divided along racial lines, and for some of the poorest of the poor, times are even harder now than they were under white minority rule. The top 20% of families make 60% of the money in South Africa. The bottom half of families take home only 15% of the wealth. The unemployment rate for black South Africans is 41.2%, among the worst in all of Africa. White South Africans have an unemployment rate of 5.1%, among the best in the developed world. 17.1% of South Africans of Indian descent are out of work, while 19.8% of the mixed-race or 'colored' population is unemployed.

Even more significant, in terms of hope for the future, 51.4% of youths aged 16 to 24 are unemployed. That means that once young people graduate or drop out of school, more than half of them are unable to find work. Many of these young people turn to black-market activities, such as the drug trade or prostitution, or support themselves through robbery and violent crime. South Africa is also losing the next generation of workers and leaders, while the very wealthy fear for their property and lives in the face of one of the world's worst epidemics of serious crime.

The average black worker makes 12,000 Rand per year (US$1525). A white worker averages 65,400 Rand (US$8,270). 18% of black households have running water, while 87% of white households do. 95% of white families have a telephone, and 46% own a computer. For black families, 31% have a phone, and less than 2% have a computer. Many black families scrape by on US$3 or less per day. They struggle to scrape together the US$25 yearly school fees for their children.[143] In a setting like this, tax revenue is of course extra important to redistribute wealth and give people access to healthcare, education and other basic needs, and the consequences of revenue loss even greater than in a society with less inequality.

Civil society, research, and future needs

A large part of the South African NGOs connected to issues concerning capital flight look at South Africas' resource bases and are mainly mining oriented, such as South African Resource Watch.[144] The others conduct budgetary work like the Institute for Democracy in Southern Africa (IDASA) [145] This includes thematic based analysis such as the South African Women's Budget Initiative[146], who analyse the budget from the perspective of gender-based analysis. In addition, there have been some anti-poverty programmes such as the People's Budget 2006-2007, the Congress of South African Trade Unions, the South African Council of Churches, and the South African NGO Coalition.[147]

In addition, the Institute of Security Studies[148] has begun working in the area of money laundering and organised crime, not only in South Africa but also in eastern and central Africa. The Institute provides information and analysis of serious organized and cross-border crime patterns in Southern, Western and Eastern Africa to inform about counter-measures at an appropriate level. It studies criminal business in Africa, particularly organized crime, money laundering and the funding of terrorist activities, in order to advise and support institutions of government and parliaments, the private sector, and other interested parties on policies and measures to reduce these forms of crime.[149]

There is already some research being carried out on capital flight. But there is still a need for more in-depth and detailed knowledge on how banks are involved in capital flight both into and from South Africa, as well as how the tax haven provisions are utilised at the national, regional as well as continental and international levels by both residents and non-residents.

At the national level, there is a need to continue to strengthen the understanding of both citizens and policy makers of effects of capital flight on the individual South African, as well as the overall development needs of the state. In addition, there is a need to take the legislation a step further and pursue its effective and efficient enforcement. It should be investigated whether the current framework of guidelines are sufficiently addressing the particular context of the South African economy which is (a) cash based, and (b) where informal value transfer methods are the norm. NGOs and the media may play an important role in informing civil society of tax evasion and avoidance and corrupt actions by publishing knowledge that is made easily available for the public.

TANZANIA

Prepared by the Budget Working Group of Policy Forum in Tanzania

Country facts	
Population, total	*43.7 million (2009)*
GDP per capita	*US$ 509 (2009)*
Life expectancy at birth, total	*55.6 years (2009)*
Child malnutrition	*17% of children under 5 (2008)*
Literacy	*72 % of population age 15+ (2008)*
Mobile cellular subscriptions per 100 people	*31 (2008)*
Internet users per 100 people	*1.2 (2008)*
Total debt outstanding and disbursed	*US$ 5.9 billion (2008)*

The agricultural sector plays a major role in the economy and employs nearly 80% of the workforce. The most important export commodities are gold and other minerals, industrial products, tobacco, coffee, cotton, cashew nuts, tea and spices. Key growth sectors are mining construction, manufacturing and tourism.

Reaching the Millennium Development Goals remains elusive even in areas such as income poverty and access to safe drinking water, which were previously considered within reach[150].

Introduction

Over the past years, the government of Tanzania has focused on raising revenue from a limited number of sources. The focus has been on taxation on drinks, fuel, cigarettes and tobacco products, as well as Value Added Tax and Pay as You Earn (PAYE). The current general consensus amongst the citizens is that these sectors are already overtaxed and that the government cannot impose any further taxes in these areas without aggravating the already rising costs of living and sinking the population further into poverty. The emerging question, therefore, is from where else can government raise more money?

In this case study, an analysis based on the available international trade data is made by Policy Forum in Tanzania. It indicates that the Tanzanian government can raise more revenue for the budget by blocking the current massive revenue outflow rather than relying on foreign aid, or over taxation of a few limited sectors.

The case study provides an overview and analysis of the Tanzanian government's revenue based on the projections for the 2009/2010 national budget. It presents some of the data as provided in the Budget Guidelines and Budget Framework for 2009/10-2011/12, which indicates that government revenue will decline steadily until the end of 2012. The study highlights some of the challenges the government will face in light of reduced tax revenues in the wake of the global economic financial crisis, but also gives insight with regards to how much revenue Tanzania loses through mispricing (for an explanation of mispricing see page 17-18) and uncollected tax.

Government's revenue, aid and debt projections

Tanzania's domestic revenue collection in the 2008/2009 fiscal year saw a *10 percent* shortfall in meeting its target, and domestic revenue will drop further in 2009/2010 due to the global economic slump. The Government's projection is that revenue for the year 2009/2010 is expected to fall until the end of 2012, as is foreign assistance. The overall resource envelope will decline by 4% of GDP from 2008/9 to 2011/12. This is primarily due to a projected decline in foreign assistance.

	2008/09	*2009/10*	*2011/12*
Domestic revenue *(% of GDP)*	17.7%	17.0%	17.5%
Foreign assistance *(% of GDP)*	9.1%	8.9%	5.3%
Overall resource envelope *(% of GDP)*	26.8%	25.9%	22.8%

Projections according to Government Budget Guidelines

At the same time, the government has committed itself to continue a policy of zero domestic borrowing for budget financing over a medium term expenditure framework period. This means that the government has to look to other sources of revenue to cushion its dwindling current sources.

Expenditures and plans for domestic resource mobilisation

During the 2009/2010 financial year, the government projects the total government expenditure to *Tsh 9.5 trillion (approximately US$ 6.3 billion[151])*. This compares to a slight increase in the government's overall budget frame since the previous year, but is a decline in real terms if factoring inflation. According to the following table, the total, recurrent, and development expenditures will fall persistently during 2008-2012. This is consistent with the government's intention of financing the recurrent expenditure from domestic revenues, while steadily building its savings for financing infrastructure projects from domestic sources.

	2008/09	*2009/10*	*2011/12*
Total expenditure *(% of GDP)*		25.9%	22.8%
Recurrent expenditure *(% of GDP)*	17.7%	16.8%	15.6%
Total development expenditure *(% of GDP)*	9.3%	9.1%	7.3%

Expenditures according to the Budget Guidelines and Medium Term Expenditure Framework (MTEF)

From this data, it is evident that over the next years the government will grapple to manage its budget. As a consequence, its macroeconomic targets may not be achieved. In order for the government to raise these funds, new innovative choices have to be made. According to government plans, the focus for the 2009/2010 budget will be to direct efforts in the following areas:

- Improving tax administration and accountability among the taxpayers and tax collectors
- Widening of the tax base by registering new taxpayers and improving tax compliance
- Instituting improved management and control of tax exemptions
- Establishing additional Large Taxpayers Units for medium sized taxpayers in order to facilitate collection of more revenue in the medium term
- Automating the tax system
- Strengthening supervision of excise and customs duties
- Increasing the contribution of non-tax revenue from the current level of about 1 percent of GDP to at least 3 percent of GDP in the medium term.
- Tapping into resources accumulated as revenue from surpluses, dividends and corporate tax from public investments by making changes in the Finance Act of 2008.

Despite these good initiatives, experience in the past years indicates that the government's seemingly good plans have never successfully generated resources to meet its anticipated national targets. The revenues generated from the government's fiscal and monetary plans are still far below the actual revenue required to finance and achieve Tanzania's national development strategy known as MKUKUTA targets.

Achieving the MKUKUTA targets (Tanzania's national development strategy)

MKUKUTA is a Kiswahili acronym for the National Strategy for Growth and Reduction of Poverty. It forms part of Tanzania's efforts to deliver on its national Vision 2025. The focus is outcome-orientated and organized around three clusters:

Cluster 1: Growth and reduction of income poverty

Cluster 2: Improved quality of life and social well-being

Cluster 3: Governance and accountability[152].

According to the Budget Guidelines, the total amount of money required (requirements) to achieve these targets in 2009-2010 is *Tsh 5.8 trillion*. The actual resources available (ceilings) to the government is *Tsh 3.6 trillion*. Hence, the difference between the total requirement and ceilings (MKUKUTA funding Gap) is *Tsh 2.2 trillion (approximately US$ 1.5 billion)*. Faced with this shortage, the government has had to make very calculated manoeuvres by thinly spreading the available revenue resources across the three MKUKUTA clusters.

The consequence of this scarcity of resources to meet high targets is that the net impact of MKUKUTA has not been adequate to bring about changes in the lives of ordinary citizens. This therefore implies that the government has to look elsewhere to generate more revenue to finance and achieve its MKUKUTA targets. Faced with an already over taxed population and a shrinking source of foreign aid, the logical alternative for the government is to look into the massive revenue that has been lost through illicit conduit means.

Revenue loss arising from illicit capital flight and tax evasion

According to estimations from Global Financial Integrity, illicit capital flight from Tanzania was on average US$ 660 million per year between 2002-2006[153]. The total illicit capital flight between1970-2008 is estimated at US$7.356 billion[154].

Mining companies in Tanzania have engaged in aggressive tax evasion measures aimed at reducing their tax obligation. Tax evasion is an illegal practice, where companies knowingly under declare their profits to lower their tax bill (see an explanation on page 17-18). In 2003, an independent auditor contracted by the government to examine the account of four major Tanzanian gold mining companies alleged that two of them over declared their losses, reducing in turn their tax liabilities to the government. If the auditors report is correct, this has cost the government Tsh 171 billion (equivalent to *US$132 million*) in lost revenues between 1998 and 2003.

According to international trade statistics, Tanzania lost approximately *Tsh 53.93 billion (approximately US$ 36 million)* in revenue due to illicit means and trade mispricing of Tanzanian products sold to foreign countries between 2005 and 2007[155]. Still, this is a crude figure because it only combines the cumulative revenue estimates lost to the European Union and the United States. The loss excludes revenue lost in trade with trading partner countries like China, India and South Africa. It also excludes revenue lost due to bad contracts in lucrative sectors such as mining, fishing, forestry and tourism. During this period, revenue loss was increasing significantly each year. Another estimation of revenue loss due to trade mispricing made by Global Financial Integrity shows that Tanzania on average lost US$ 32.7 million per year between 2002-2006[156].

Data from the United Nations database Comtrade, Eurostat and the US census board - which contains data on the quantity and value of commodity trade between countries (if reported by one of these countries) - indicates that there is a significant variation between the quantity and values of the commodity trade between Tanzania and other countries. The massive loss of revenue is largely due to multinationals evading taxes through a system called *transfer pricing and trade mispricing (explained on page 17-18)*. This system includes under pricing, transfer of profits and establishment of subsidiaries of multinationals in *tax havens* like the Canary Islands, Jersey, Island of Man and Cayman Islands to avoid paying taxes in countries such as Tanzania. The impact of such tax evasion on Tanzania's economy is great as the country is badly deprived of the much needed revenue.

The trade data between 2005-2007 indicates that Tanzania is the second largest loser of revenues due to trade mispricing in the East African region. Kenya loses the largest volume of revenue to the European Union and United States, while Uganda follows in third place. One of the explanations for this trend is that Kenya is the biggest economy in the region. But another explanation is that most of Tanzanian products are smuggled into Kenya and sold as Kenyan products on to the international market. The international trade statistics therefore record this volume of trade as originating from Kenya. The major products smuggled from Tanzania into Kenya include agricultural, mining and tourism.

Revenue loss arising from tax exemptions

Tanzania is also losing massive revenue in tax exemptions and tax breaks granted to government departments, donor supported projects, private businesses, NGOs and mining companies. This is not illegal and is not the same thing as illicit capital flight, but should be mentioned because of the huge revenue loss it incurs to the country. According to the Tanzanian revenue authority, the Government lost Tsh *587 billion* in tax exemptions made between July 2008 and April 2009. Projects under the Tanzania Investment Center (TIC) accounted for the largest percentage of the total exemption. Other beneficiaries included state-owned institutions, the government of Zanzibar, as well as religious and non-religious non-governmental organizations. In 2008 alone the government lost *Tsh 1.8 trillion* in exemptions (approximately US$ 1.2 billion).

More revenue was lost to mining companies operating in Tanzania. None of the mining companies have sought exemptions from royalties or corporate income taxes in any of the contracts. However, they have sought significant exemptions from local government taxes, withholding taxes, and fuel levies. The mining agreements stipulate that companies will not pay local government tax in excess of US$ 200,000 a year (Tsh 260 million), even though this is much lower than the 0.3% of the value of company turnover, which the law requires they should pay in local government taxes.

The Bomani Commission has estimated that the government has foregone Tsh 39.8 billion (approximately US$ 26.5 million) in 2006/2007 and Tsh 59 billion in 2007/2008 in revenue as a result of fuel levy exemptions granted to the six largest mining companies. In addition, the mining contracts have set stamp duties at 0.3%, a tenth of the rate of 4% stipulated in the substantive law.

The revenue lost through a combination of tax exemptions and illicit trade means such as trade mispricing with foreign countries and multinationals amounts to over *Tsh 2 trillion* a year. This amount would have gone a long way to cover the financing gap of *Tsh 2.2 trillion (approximately US$ 1.5 billion)* required to meet the MKUKUTA cluster requirements for the year 2009/2010.

Recommendations specific to Tanzania

In order for the government to achieve its stated policy objectives, measures should be taken according to the general recommendations on page 66-67. Efforts that are specific for the Tanzanian context should be directed in the following areas:

- We commend the government's plan to improve tax administration by implementing the TRA's Third Corporate Plan, which focuses on promoting compliance and accountability among the taxpayers and tax collectors.
- Locally curbing mispricing by enacting legislation demanding transparency and accountability by multinational companies and foreign governments doing business with Tanzania. Company law in Tanzania should require all registered mining and other extractive companies to use the EITI template in reporting on their annual financial operations.
- Seeking the possibility of using Tanzania's influence in the United Nations Security Council to lobby for establishment of an international Tax Police system modelled around the global police body Interpol (which combats transnational crime) and the Kimberly certification process (which monitors global trading in blood diamonds). This process would involve getting exporting countries or countries of origin to certify that a given set of goods have been exported with due consideration of the country's tax laws.
- Addressing the indiscriminate and uncalled for tax exemptions and subsidies which are fleecing the government of much revenue to finance its operations. The best option for exemption should be case-by-case rather than blanket exemptions to all state institutions, donor supported projects, religious organizations, NGOs and private investments. The exemption and tax waiver policy for large multinational companies and mining companies should be reviewed.

Conclusion

As the government of Tanzania grapples to maintain financial stability to finance its budget in the face of the current global economic crisis and dwindling foreign sources, it is clear that the government faces a huge problem with tax dodging by big businesses. The same applies for uncalled for exemptions. The government can raise more revenue internally by blocking the massive losses due to trade mispricing and unnecessary exemptions, which have for so many years allowed companies and individuals to take millions of shillings meant for the Tanzanian government. The consequence of this has been declining revenue collection and declining social service delivery. This has angered the citizens and driven them further towards evading taxes. The citizens need to see improved social service delivery. Social services require revenue and government cannot achieve its targets without collecting more taxes internally. Citizens will be less likely to pay more taxes if they continue to see that large companies that are supposed to pay taxes do not.

***NOTE:** All of the data in this brief should be treated with caution, as the Budget Guidelines provide only preliminary indications of what is expected in the coming financial year. This brief is also based on the Guidelines for the Preparation of Medium Term Plan and Budget Framework for 2009/10-2010/12 ; A Christian Aid Report, entitled: False Profits: robbing the poor to keep the rich tax free, March 2009; and figures calculated based on trade statistics available at Eurostat and the US Census Board.*

SUMMARY RECOMMENDATIONS

If non-governmental organisations and decision makers in Europe and Africa act together they can reduce or end illicit capital flight. The list below sets out measures recommended from the findings in this report. Commitment at the national, regional and international level is needed to:

1. Improve the international accounting system to make it more transparent so that illicit capital flight can be uncovered. Currently, companies are not required to report enough detail about their profits, their tax payments or even their ownership to enable governments to claim the tax that is due. Multinational companies should be obliged to report their financial activities with a breakdown for each country where they operate. This is called *country-by-country reporting*. Making it *mandatory for all types of multinational companies* is a first step towards prevention of illicit cross-border flows. Governments and international groupings such as the G20 and UN should formally request the International Accounting Standards Board to adopt it in their International Financial Reporting Standards.

2. The key to tackling tax havens is to ensure that all countries require their financial institutions to reveal information on all sorts of income to tax authorities, and that such information is exchanged between states. Only through information exchange between states will it be possible to track illicit capital flight through tax evasion and avoidance, as well as criminal activities and corruption. To be affordable and useful for developing countries, the *information exchange agreements* have to be *multilateral*, and exchange of information has to be *automatic* instead of upon request. To capture capital flight fully, the agreement must aim at being *global*, and there has to be multilateral countermeasures for non-compliance. Ongoing discussions at the G20 and OECD should result in this. *Sanctions should be imposed on tax havens* that do not actively cooperate on information exchange.

   If needed and wanted, donors should provide support for developing countries to develop their technical capacity (including the requirements for confidential handling of information) so that they can adhere to a multilateral agreement on automatic information exchange.

3. *African states need to strengthen their tax systems, surveillance, and collection of tax* to prevent tax evasion and illicit capital flight. *EU states must support capacity building* of tax authorities in African states. This should include technical assistance and expertise, specifically to customs, revenue and bank supervisory authorities. It should be available to African countries that request it, for them to purchase from a service provider of their choice. Donors should make specific efforts aimed at *recovering and repatriating stolen assets* to African states.

4. To include all countries in the work against illicit capital flight, *the United Nations Committee of Experts on Tax Matters should be strengthened and upgraded with a political mandate* to an intergovernmental body. A main task for the committee should be to develop and promote the *UN Code of Conduct on International Cooperation in Combating Tax Evasion*, which should be implemented at the national and international level. Non-governmental organisations are calling for the committee to establish tax avoidance and tax evasion as a form of corruption.

5. States should adopt *codes of conduct by tax administrations* which make clear that tax evasion and avoidance is unacceptable, as well as ensure disclosure of information and fiscal cooperation aimed at eliminating bank secrecy.

6. States should *take legal action on illicit capital flight*. The handling of the proceeds of illicit capital flight, and aiding and facilitating illicit capital flight, should be made a crime with strict penalties that might include suspending a bank's banking licence and revoking the license to practice of accountants, lawyers and other professionals. Criminal penalties should also be considered in the most egregious cases of abuse.

7. Because of the link between illicit capital flight and debt, responsible lending and borrowing has to be ensured. This could be done, for example, through applying the *responsible financing standards* developed by Eurodad when signing a loan. This ensures transparency, shared responsibility between borrowers and lenders, and fair arbitration if responsibilities are not honoured.

8. Governments that are on the board of the *World Bank and the International Monetary Fund should* ensure that the institutions do *not pressure governments to liberalise capital controls, sector regulations or other economic policies* in such a way *that will permit greater capital flight.*

9. *Public funds intended for development should not be allowed* to benefit tax havens and facilitate illicit capital flight trough *making use of tax havens*. Research has shown that national aid agencies, investment funds for development, and the International Finance Corporation at the World Bank make use of tax havens or support companies that make use of tax havens. This should not be allowed. Companies that benefit from support should be obliged to report their financial activities on a country-by-country basis.

10. There is a lack of information on and awareness of illicit capital flight and its effects on development. Donors should *support research* by academics, as well as *surveillance and awareness raising* by civil society organisations.

APPENDIX

INSTITUTIONS AND SOURCES OF INFORMATION ON CAPITAL FLIGHT FROM AFRICA

Currently there are several initiatives at state, national, regional and international levels dealing with capital flight from Africa. They include:

	Initiative/Actor	*Description*	*Link*
1	Action Aid	Antipoverty NGO that has been engaged in issues on tax evasion and international financial structures.	*www.actionaid.org*
2	AFRODAD	African Forum and Network on Debt and Development, Network of African NGOs.	*www.afrodad.org*
3	African Development Bank	The bank has an anti-corruption initiative and works to prevent money laundering.	*http://www.afdb.org/en/topics-sectors/sectors/economic-financial-governance/anti-corruption-initiative/#*
4	Bank for International Settlements (BIS)	International organisation which fosters international monetary and financial cooperation and serves as a bank for central banks.	*www.bis.org/*
5	Basel Committee on Banking Supervision (BCBS)	Provides a forum for regular cooperation on banking supervisory matters.	*www.bis.org/bcbs/index.htm*
6	Basel Institute on Governance	Independent non-profit institution devoted to interdisciplinary research, policy advice and capacity building in the areas of public, corporate, and global governance (Centre for Governance and Research), and offers special services in the field of asset recovery (International Centre for Asset Recovery).	*www.baselgovernance.org/*

	Initiative/Actor	*Description*	*Link*
7	Christian Aid	International NGO working to fight poverty. Illicit financial flows and tax evasion are addressed in several publications.	*www.christianaid.org.uk/*
8	Committee on Payment and Settlement Systems (CPSS)	Aims to strengthen the financial market infrastructure through promotion of sound and efficient payment and settlement systems.	*www.bis.org./cpss/index.htm*
9	Committee on the Global Financial System (CGFS)	Monitors developments in global financial markets for central bank governors.	*www.bis.org/cgfs/index.htm*
10	CRADEC	Centre Régional Africain pour le Développement Endogène et. Communautaire (Cameroon).	*No website*
11	Eastern and Southern Africa Money Laundering Group (ESAAMLG)	Membership organisation for jurisdictions in Eastern and Southern Africa working together for prevention and control of the laundering of the proceeds of serious crimes.	*www.esaamlg.org/*
12	Egmont Group For Financial Intelligence Units (FIUs)	Informal international association of FIUs.	*www.egmontgroup.org*
13	Financial Action Task Force on Money Laundering (FATF)	Intergovernmental body whose purpose is the development and promotion of national and international policies to combat money laundering and terrorist financing. FATF 40+9 recommendations call for countries to operate FIUs that meet the Egmont Group's definition.	*www.fatf-gafi.org*
14	Financial Stability Board	Established to address vulnerabilities and to develop and implement strong regulatory, supervisory and other policies in the interest of financial stability.	*www.financialstability-board.org/index.htm*

	Initiative/Actor	*Description*	*Link*
15	Forum Syd	A network of over two hundred Swedish organisations working with international development cooperation and advocacy on global issues with the common aim of global justice. Forum Syd has offices in Nairobi and Muanza.	*www.forumsyd.org*
16	Global Financial Integrity (GFI) and the Task Force on Financial Integrity and Economic Development	Promotes national and multilateral policies, safeguards, and agreements aimed at curtailing the cross-border flow of illegal money. The Task Force on Financial Integrity and Economic Development, initiated by GFI in 2009, is a coalition of civil society organisations and governments that work to address inequalities in the financial system.	*www.gfip.org/*
17	Global Witness	NGO which investigates and campaigns to prevent natural resource-related conflict and corruption.	*www.globalwitness.org*
18	International Monetary Fund (IMF)	Publishes assessments of financial sectors in African countries and engages in anti-money laundering and combating the financing of terrorism.	*www.imf.org/external/np/leg/ amlcft/eng/aml1.htm#custom er*
19	IMF and the World Bank	Financial sector assessment programme (FSAP). The programme brings together World Bank and IMF expertise to help countries reduce the likelihood and severity of financial sector crises.	*www.worldbank.org/fsap*
20	Information Portal on Corruption in Africa	Online resource portal on anti-corruption and democratic governance in Africa.	*www.ipocafrica.org*
21	Institute for Security Studies (ISS)	Applied, policy-oriented research institute operating across Sub-Saharan Africa. The Cape Town branch of ISS runs two major programmes on 'Organised crime and money laundering' and 'Governance and anti-corruption'.	*www.issafrica.org*

	Initiative/Actor	*Description*	*Link*
22	Institute for Economic Affairs	NGO formed to promote informed debate on key policy issues, both economic and political, and to propose feasible policy alternatives in these areas. In addition, the institute provides research backup to policy makers including members of parliament.	*www.ieakenya.or.ke*
23	Inter Governmental Action Group against Money Laundering in West Africa (GIABA)	An intergovernmental body whose purpose is the development and promotion of policies, both at national and international levels, to combat money laundering and terrorist financing.	*http://www.fatf-gafi.org/document/60/0,3343,en_32250379_32236869_34393596_1_1_1_1,00.html*
24	International Organization of Securities Commissions (IOSCO)	Membership organisation for jurisdictions to promote high standards, integrity and collaboration on market development.	*www.iosco.org*
25	Interpol	The world's largest international police organisation, with 188 member countries. Facilitates cross-border police cooperation, and supports and assists all organisations, authorities and services whose mission is to prevent or combat international crime.	*www.interpol.org*
26	ISODEC	NGO working for sustainable human development through the empowerment of the poor and other marginalised groups, especially women.	*www.isodec.org.gh*
27	Mauritius: Financial Intelligence Unit	Financial intelligence unit.	*www.fiumauritius.org/*
28	MONEYVAL; Council of Europe	Select committee of experts on the evaluation of anti-money laundering.	*www.coe.int/t/dghl/monitorin g/moneyval/*
29	National Taxpayers Association	The NTA is an independent, non-partisan organization focused on promoting good governance in Kenya through citizen empowerment, enhancing public service delivery and partnership building.	*http://www.nta.or.ke/*

	Initiative/Actor	Description	Link
30	Nigeria: Financial Intelligence Unit	Financial intelligence unit.	www.efccnigeria.org/index.php?option=com_docman&task= cat_view&gid=18
31	Oxfam Novib	NGO working to fight global poverty and to build independent livelihoods in developing countries.	www.oxfamnovib.nl/
32	Organisation for Economic Coordination and Development (OECD)	Involved in most aspects concerning the fight against illicit financial flows, anti-corruption, tax evasion, money laundering, terrorist financing and asset recovery. The web page is a resource for publications, statistics and information.	www.oecd.org
33	Policy Forum, Tanzania	A network of over 90 NGOs registered in Tanzania, drawn together by their specific interest in influencing policy processes to enhance poverty reduction, equity and democratization.	www.policyforum-tz.org
34	South Africa: Financial Intelligence Centre (FIC)	Financial intelligence unit.	www.fic.gov.za/
35	Stolen Asset Recovery Initiative (StAR)	Partnership between the United Nations Office on Drugs and Crime (UNODC) and the World Bank. Aims to encourage and facilitate more systematic and timely return of assets stolen by politically exposed persons through acts of corruption.	http://www1.worldbank.org/publicsector/star_site/
36	SOMO	Centre for Research on Multinational Corporations.	http://somo.nl/
37	The Norwegian Government's Expert Commission of Inquiry into Capital Flight from Developing Countries	Expert commission on tax havens and development.	http://www.regjeringen.no/en/dep/ud/press/news/2009/pm_taxhavens.html?id=567661

	Initiative/Actor	*Description*	*Link*
38	Tax Research Limited	Private company researching and advising on tax issues and other aspects of governance. Directed by chartered accountant Richard Murphy.	*www.taxresearch.org.uk/*
39	Tax Justice Network	Independent organisation which conducts research, analysis and advocacy in the field of taxation and regulation, including the developmental impacts of tax evasion and tax havens.	*www.taxjustice.net*
40	Tax Justice Network-Africa	African Secretariat of the Tax Justice Network.	*www.taxjustice4africa.net*
41	International Money Laundering Information Network (IMoLIN)	Internet-based network of organisations and individuals.	*www.imolin.org/*
42	U4	Anti-corruption resource centre serving bilateral donors. Located at Chr. Michelsen Institute, Norway.	*www.U4.no*
43	United Nations Office on Drugs and Crime (UNODC)	Operates in all regions of the world through an extensive network of field offices. Mandated to assist member states in their struggle against illicit drugs, crime and terrorism through technical cooperation and analytical work.	*www.unodc.org*
44	US Senate Permanent Subcommittee on Investigations	Investigation of cases linked to the U.S.	*http://hsgac.senate.gov/public/indcfm?FuseAction=Subcommittees.Investigations*

TAX HAVENS, OFFSHORE FINANCE CENTRES AND SECRECY JURISDICTIONS ACCORDING TO OECD, IMF, TAX JUSTICE NETWORK AND THE FINANCIAL SECRECY INDEX RANKING

Tax havens, offshore finance centres and secrecy jurisdictions	*OECD-list*	*IMF-list*	*TJN-list*	*Financial Secrecy Index Rank*
Andorra*	X	X	X	57
Anguilla*	X	X	X	joint 55
Antigua & Barbuda*	X	X	X	joint 46
Aruba	X	X	X	36
Austria				12
Bahamas	X	X	X	33
Bahrain	X	X	X	14
Barbados		X	X	28
Belgium			X	9
Belize	X	X	X	37
Bermuda	X	X	X	7
British Virgin Islands	X	X	X	16
Brunei*				joint 39
Cayman Islands	X	X	X	4
Cook Islands*	X	X	X	joint 46
Costa Rica		X	X	34
Cyprus	X	X	X	18
Dominica*	X	X	X	joint 39
Germany (Frankfurt)			X	
Gibraltar*	X	X	X	joint 46
Grenada*	X	X	X	joint 46
Guernsey	X	X	X	13
Hong Kong		X	X	10
Hungary			X	22
Iceland			X	
Ireland		X	X	6
Isle of Man	X	X	X	24
Israel (Tel Aviv)			X	20
Italy (Campione d'Italia & Trieste)			X	
Jersey	X	X	X	11
Latvia				26
Lebanon		X	X	27
Liberia*	X		X	54
Liechtenstein*	X	X	X	joint 55
Luxembourg		X	X	2
Macao		X	X	29
Malaysia (Labuan)		X	X	23

Tax havens, offshore finance centres and secrecy jurisdictions	*OECD-list*	*IMF-list*	*TJN-list*	*Financial Secrecy Index Rank*
Maldives*			X	58
Malta	X	X	X	21
Marshall Islands*	X	X	X	joint 46
Mauritius	X	X	X	32
Monaco*	X	X	X	60
Montserrat*	X	X	X	59
Nauru*	X	X	X	joint 46
Netherlands			X	15
Netherlands Antilles	X	X	X	38
Niue	X	X	X	
Northern Mariana Islands			X	
Palau		X		
Panama	X	X	X	19
Philippines				25
Portugal (Madeira)			X	17
Russia (Ingushetia)			X	
Samoa*	X	X	X	joint 39
San Marino	X			
São Tomé e Principe			X	
Seychelles*	X	X	X	joint 39
Singapore		X	X	8
Somalia			X	
South Africa			X	
Spain (Melilla)			X	
St Kitts & Nevis*	X	X	X	joint 46
St Lucia*	X	X	X	joint 39
St Vincent & Grenadines*	X	X	X	joint 39
Switzerland		X	X	3
Taiwan (Taipei)			X	
Tonga			X	
Turkish Rep. of Northern Cyprus			X	
Turks & Caicos Islands*	X	X	X	joint 39
United Arab Emirates (Dubai)			X	31
United Kingdom (City of London)			X	5
Uruguay			X	30
US Virgin Islands*	X		X	joint 46
USA (Delaware)				1
USA (New York)			X	
Vanuatu	X	X	X	35

** Jurisdictions marked with an asterix are ranked according to their opacity score.*

Source: Tax Justice Network (2007), Identifying tax havens and offshore finance centres

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BRINGING THE BILLIONS BACK

Every year huge unreported flows of money are leaving developing countries, ending up in rich countries or tax havens. If properly reported, this illicit capital flight would generate at least US$160 billion per year in tax revenue - more than one and a half times the total annual aid to the developing world. These are resources that could be crucial in the fight to combat poverty.

Contrary to popular belief, only a small share, three to five percent, of illicit capital flight stems from corruption. Instead, almost two thirds originate from multinational companies evading to pay tax, and one third is a result of criminal activities such as trade with humans, drugs and weapons. Despite the fact that illicit capital flight has severe consequences for developing countries – it cancels investment, undermines trade, hurts competition, worsens income gaps and drains hard-currency reserves – awareness of the measures needed to end it is low.

As a percentage of GDP, capital flight from Africa is larger than from other parts of the world. But Africa cannot stand alone to stop it, cooperation and political will is required by decision makers in Europe as well as in Africa.

This report explains illicit capital flight, how it happens, its magnitude, its consequences for the poor, and measures needed to end it. It also presents illustrative case studies from Kenya, South Africa and Tanzania.

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