Opportunities and Challenges that Promote the Advocacy Efforts for the Legal Profession

A Toolkit on Illicit Financial Flows: Module 1

Politics of Defining Illicit Financial Flows
About the project:
As a unique space under the Financial Transparency Coalition (FTC), the Southern Regions Programme (SRP) plays a crucial role of an incubator by placing just tax systems and financial transparency at the heart of development debates. In October 2017, during a South-South strategy meeting it was recognised to bring out a collaborative document that emerged from the perspective of the Global South. Five members of the SRP came together to author the IFF Toolkit in an effort to address issues of financial secrecy, enablers of illicit financial flows, lopsided impact on domestic resources and the ability to raise further resources due to loss of revenue as IFFs and the much-needed reforms in the international financial architecture set in the context of Global South. The toolkit uses case study-based evidence to simplify the issue of tax abuse. The document also covers tax incentive abuse as a subject under IFFs. The toolkit has benefitted from discussions held at the Nepal Social Forum (March 8th-10th, 2018), Paper on Illicit Financial Flows: Rights, Restoring Justice and Freedom and Pan-Continental Southern Dialogue on Illicit Financial Flows², Nairobi (November 21st-22nd, 2018).

Disclaimer:
The publication has been produced by Centre for Budget and Governance Accountability (CBGA), Latin American Network on Economic and Social Justice (LATINDADD) and Tax Justice Network Africa (TJNA) who together form a part of the Southern Regions Program in the Financial Transparency Coalition (FTC). This output does not intend to reflect the positions of all members of FTC.

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1 Asian People's Movement on Debt and Development (APMDD), Centre for Budget and Governance Accountability (CBGA), Latin American Network on Economic and Social Justice (LATINDADD), Pan African Lawyers Union (PALU) and Tax Justice Network Africa (TJNA)

List of Acronyms

ACBF  African Capacity Building Foundation
AFRODAD  African Forum and Network on Debt and Development
AU  African Union
AUC  African Union Commission
CoDA  Coalition for Dialogue on Africa
ECA  Economic Commission for Africa
ECLAC  Economic Commission for Latin America and the Caribbean
FID  Financing for Development
HLP  High-Level Panel
IFCF  Illicit Financial Cumulative Flow
IFFs  Illicit financial flows
MNCs  Multinational corporations
SDG  Sustainable Development Goals
UNECA  United Nations Economic Commission for Africa

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Countries lose huge sums of revenue as illicit financial flows. But what are they?

To understand this phenomenon, we look into how trade routes were established during the colonial period via "tax havens" giving rise to the present economic system. Used to hide one's wealth, "tax havens" have evolved as offshore/onshore hubs of secrecy for businesses, oligarchs and the corrupt. Apart from offering low or no taxes to corporations, "tax havens" also provide a shelter from other necessary rules and regulations set in place by oversight bodies. Naturally, these jurisdictions or hubs are central in facilitating illicit financial flows or IFFs.

The entire concept of IFFs emerged as "capital flight" in response to the deregulation waves and the debt crises in developing countries in the 1980s after the oil shocks sent interest rates soaring, hitting the currencies and economies of the Global South. The discussion at the time was mostly had in institutions based in the Global North, who saw capital flight as a result of the loss of investment climate and economic confidence of residents of the country. It was assumed that unrecorded capital flight or mispriced trade was mainly due to differences in methods of recording balance of payments or trade transactions.

In fact, the first instance of framing capital flight as "illicit" was discussed by Bhagwati (1964) and then in 1974 by Bhagwati, Krueger, Wituswadia, where illegal capital flight was defined as the undocumented capital transacted either by deliberately under-invoicing exports and/or over-invoicing imports, or faking of trade documents.
as a consequence of exchange controls in the Global South. From then a literature on illegal and illicit capital flight emerged, which pointed out corruption and tax evasion as motives for capital flight—trying to figure how much of this capital flight was in fact criminal or abusive activity, and what proportion was in some way legitimate. The seminal study that showed the vast majority of capital flight was illegitimate in a number of cases was the paper by Boyce and Ndikumana (2001). They linked a number of debt crises to a dynamic where the corrupt elites stole the money raised in the form of debt into personal gain, thus causing illegal capital flight.

Initially Boyce and Ndikumana looked only at capital account movements that were unrecorded, with the assumption that if something is not recorded it is likely to be due to the illicit nature of the transaction. Subsequently, with trade data being analysed, it was added that trade mispricing should also be considered an illicit financial flow if there are mismatches. Building on their work, Baker (2003, 2005) coined ‘dirty money’ for capital that is illicit in its origin, transit or destination. This, later on, has become the narrowly conceived definition of Illicit Financial Flows mainly focusing on ‘illegality’ of financial flows (Kar and Cartwright-Smith, 2006). The legalistic conception minimises the larger systemic aspects of the problem. Therefore, it is also important to include tax-related flows like profit-shifting and tax abuse (tax avoidance, tax dodging and tax evasion) under the ambit of IFFs.

The term illicit financial flows became an intergovernmental issue with the convening of the 4th Joint AU Commission / UN Economic Commission for Africa (AUC/ECA) Conference of African Ministers of Finance, Planning and Economic Development in 2011. With newer research, the term includes capital income derived from undeclared offshore wealth held often in tax havens. We arrive at a matrix of data and case-study evidence that structure the understanding of illicit financial flows.

The next few sections adddress the different components of IFFs to arrive at a progressive definition through discussions on progress made in developing regions.

### Table 1: Illicit Financial Flows related capital losses and revenue losses

<table>
<thead>
<tr>
<th>Factor</th>
<th>Estimate 1</th>
<th>Estimate 2</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Trade mispricing</strong></td>
<td>$940-1,690 bn*</td>
<td>$3,192 bn*</td>
</tr>
<tr>
<td>Capital flight loss</td>
<td>$158-317 bn*</td>
<td>$58 bn*</td>
</tr>
<tr>
<td><strong>Offshore wealth</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital stock loss</td>
<td>$58 bn*</td>
<td></td>
</tr>
<tr>
<td>Tax revenue loss</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Corporate tax abuses</strong></td>
<td>$200 bn*</td>
<td></td>
</tr>
<tr>
<td>Tax revenue loss</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Notes:
1* Global Financial Integrity, January 2019, low-end estimate is trade mispricing using IMF DOTS-based estimate, while high-end estimate is the UNCTAD COMTRADE-based estimate.
2* Global Financial Integrity, June 2019a; Global Financial Integrity, June 2019b; Global Financial Integrity, June 2019c; these three studies of tax losses arising from trade mispricing give a range of 16.9% in Egypt to 17.6% in India and 18.8% in Indonesia. We use the lowest estimate and IMF DOTS low-end trade mispricing estimate for $158 billion, while highest 17.7% and high-end COMTRADE-based method for $317 billion.
3* Zucman (2017), here we have the total wealth offshore figure of $8,700 billion, of which we exclude high-income countries according to the 2019 World Bank classification to arrive at $3,192 billion for countries in the Global South.
4* Zucman, Alesina and Javorcik (2019) for method of calculating revenue loss from the offshore stock of capital, using data from Zucman et al we disaggregate the share of countries in the Global South to include 52% of Asian offshore wealth (excluding high-income Asian countries), all of Latin American and Caribbean countries, all of African countries and Russia as it is in 2019 classified by the World Bank an upper middle-income country.
5* IMF (2015)
Locating the Harm

by design, illicit financial flows disproportionately impact developing countries as they widen financing gaps and prevent any fair redistribution of resources. IFFs emerge from “financial activities and practices that are illegal or abusive” and elusive in nature with a cross-border impact. This includes activities like tax abuse, use of exploitative bilateral or multilateral tax, trade and investment agreements, harmful tax incentives, abusive transfer pricing, odious debt, trade misinvoicing, crime, bribery, corruption among others—using national and international instruments, agreements and structures and corruptible legal and political domestic environments. Poorly planned policies and agreements while may be adhering to the law still provide a basis for abusive practices. When unpacking domestic environments backed by governments, Arun Kumar (1999) describes the predominant role of systemic drivers. Policymakers, businesses and the executive together form a working triad of political class that generate illicit money. Over the years, massive investigative revelations like the Swiss leaks, Panama Papers, Mauritius leaks etc. have brought public attention on their role as facilitators of IFFs.

Secrecy keeps these funds out of the public and state eye by continuously eroding accountability. Disguised in licit circles of finance, more often than not, abusive practices do not get investigated timely due to the lack of administrative or immediate technical and fiscal resources available, especially in developing countries. Thus, contributing to the normative and theoretical debate of how IFFs have concrete socio-economic as well as judicial and political consequences especially for the South. This has led to a stronger support towards progressive definition of IFFs and its accompanying metrics.

Different Definitions and Aspects – Missing Elements

As a systemic issue, its definition and the need to unpack underlying causes are both a technical and a geopolitical debate. The standards of the international financial architecture are set by international bodies and institutions based in the Global North, which also bears effects on the sovereign rights of a developing country. These institutions aim to address different aspects of IFFs. While private firms and developed countries are members of these institutions many developing countries are not. Further, most official definitions of illicit financial flows are broad. Different actors emphasize
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Different issues of IFFs. Hegemonic powers and security-oriented UN agencies, for example, tend to focus on terrorist financing and stolen assets, while development and human-rights oriented UN agencies highlight the impact of transnational corporations’ tax dodging practices and capital flight. But civil society advocacy and recent research studies, particularly after the global financial crisis, have brought IFFs to the mainstream. Although, the debate is still dominated by Northern based institutions.

A prime characteristic of IFFs in all working definitions is the cross-border or international dimension. While few methods have tried to focus on the finances of strictly criminal activities such as drug trafficking, others do not provide estimates for “flows”, but rather for stocks of wealth—especially that are hidden in resident banks of offshore jurisdictions. It is the operationalisation of the concept that serves as a feedback for the definition itself. The need to examine the role of intermediaries, destination locations, looking for policy alternatives and the need to go beyond the legalistic definition are crucial.

Global progress on IFFs – Why is the fight geopolitical?

The transition from illegal to illicit has been a tough journey that is yet to be fulfilled. The use of the term ‘illicit’ in the definition reveals a moral or ethical lapse that needs to be addressed. Despite the issue of IFFs being on the global radar for more than 10 years, the international community has yet to agree on its definition. This lack of consensus on the definition is recognised as the most fundamental gap in being able to address the issue effectively. Consequently, the roadblock on being able to achieve a consensus has limited the discussion to drive a binary narrative of legal vs. illegal and it is this lack of clarity on the terminology that prevents sound policymaking. For example, the

### Dollars held in HSBC Swiss as a % of GDP

<table>
<thead>
<tr>
<th>Country</th>
<th>% of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kenya</td>
<td>1.08</td>
</tr>
<tr>
<td>El Salvador</td>
<td>0.36</td>
</tr>
<tr>
<td>Canada</td>
<td>0.21</td>
</tr>
<tr>
<td>El Salvador</td>
<td>4 times more as a % of GDP in SwissLeaks than Norway.</td>
</tr>
<tr>
<td>Norway</td>
<td>0.08</td>
</tr>
</tbody>
</table>

Financing for Development (FfD) negotiations too have witnessed a major opposition towards including trade misinvoicing under IFFs. Issues like debt have still not received their due consideration under IFFs. Even in the most democratic and legitimate institutions—like the United Nations General Assembly, a broad and purposefully ambiguous political consensus was attained on the issue. Nonetheless, the inclusion of the IFFs target in the UN 2030 SDG Agenda was a welcome result.

The UN Statistical Commission has identified the SDG indicator 16.4.1 on IFFs as "Total value of inward and outward IFFs (in current US dollars)" as the global metric to monitor 16.4 target of the SDGs. By including "inflows and outflows", a counterproductive interpretation (from the South's perspective) could imply that outflows are netted with inflows, and thus, the net impact of illicit financial flows is minimised. The "total" amount of inward and outward IFFs can be interpreted to mean "total net", in which case the result for the whole world (global inwards – global outwards) would be zero. Therefore, it is crucial from the perspective of the South to insist on gross estimates, for both inflows and outflows (and give less importance to the net amounts). It is also an opportunity to reflect on the fact that the South's aggregate outflows imply (by accounting identities) the North's aggregate inflows. This is a very important concept because while it may be excruciatingly complex to quantify outflows originating "IFFs", the South, it is much simpler to quantify inflows arriving in the North.

This measurement consideration is not trivial, as it assigns responsibilities to the North as facilitators, enablers and gatekeepers of IFFs.

There are other tests that reveal the illicit nature of activities by identifying illicit motives such as "market and regulatory abuse or abuse of power". Among Southern actors, the African Union Commission (AUC) and United Nations Economic Commission of Africa (UNECA) took the lead in setting a technical and a political agenda on curbing illicit financial flows in 2015 from Africa by including tax avoidance in their definition. This approach later also influenced the UN Economic Commission for Latin America and the Caribbean (ECLAC) in categorising tax avoidance. Going beyond the legal lens of viewing IFFs, the module situates this issue in the rights-based framework.

The Broken Financial System: Role of the North

Money exists, overwhelmingly, in accounting records. Accounting exists, overwhelmingly, in digital form. Unlike physical bills, which are also not trivial in IFFs and flow bilaterally, book (digital) money flows in a triangular way following the principle of double-entry bookkeeping. A debit in the sender and a credit for the receiver is mediated by a bank. If a transaction is in accounts of two different banks, a triangular five-entity bookkeeping exercise occurs in three separate ledgers. The first ledger records a debit in the sender's account and in the sender's bank's account at the central bank. The second ledger records a credit in the receiver's account and in the receiver's bank's account at the central bank. Occasionally, the third bank involved is not the central bank but another correspondent bank. If the transaction occurs internationally, other correspondent banks may be involved until a "payment chain" between the sender and receiving banks is established. Tax authorities, financial intelligence units and central banks should be overtly conscious of the fact that IFFs exist in accounting records. If the corresponding risk profiles merits the case, these authorities should be able use modern information technologies to have access to banking and corporate ledgers in real-time, and with big data, artificial intelligence and network analysis, to improve their capacities to identify IFFs.

As the Kathmandu Declaration has identified, the
The phrase “in current US dollars” itself reveals a prime characteristic of the nature of IFFs. One that they are primarily cross-border and international in nature. Two, IFFs are not usually channelled in domestic currencies and particularly not in currencies of the South. This highlights the role of central banks, together with tax authorities in recording, preventing and combating them. Therefore, a conversion of IFFs to US dollars or other “hard” currencies, such as Euros or Sterling Pounds is a necessary step. The US dollar is not only the unit of account of the UN metric, it is also the unit of account of organised crime and international taxation. This includes physical bills as it is the most frequently used currency for international transactions and thus, offshore banks.

This apparently innocuous characteristic shows how IFFs are not exclusively the responsibility of Southern countries because US dollar assets of IFF holders are, by identity, US dollar liabilities. These IFFs are recorded in the books of US banks which are ultimately connected to the US payment system. A major implication of this imbalance is that US has the power and the responsibility to inform the countries of the South of the existence and provide all details of IFFs.

The Big Picture of Global Finance in 2012

Figure 1: Top 10 Corridors for Worldwide Payments

Live, delivered international MT 103s sent in YTD September 2018

- United States - China: 16.0 (3.2%)
- United States - United Kingdom: 9.1 (12.4%)
- United Kingdom - United States: 8.8 (5.8%)
- United States - Hong Kong: 8.6 (-0.7%)
- Hong Kong - United States: 8.6 (-0.7%)
- United States - India: 8.4 (-0.7%)
- United States - Taiwan: 8.0 (-0.7%)
- Canada - United States: 7.6 (-0.7%)
- United Kingdom - Germany: 5.4 (2.8%)


National definitions:

Argentina's former (now defunct) state-led think tank CEFIAR was the most proactive quasigovernmental entity concerned with IFFs. A series of papers led by Jorge Gaggero explored definitions of capital flight and illicit financial flows. This approach has been widely adopted in Argentinian economic research circles in the statistically feasible "formación de activos externos" or "foreign asset accumulation".

access to its information on regulatory grounds, but the countries of the South—or even the UN institutions—do not.

One aspect of IFFs that may hide structural asymmetries between North and South is the temporary nature of flows. Flows are movements that happen within a time unit. The unit should specify if flows are measured as US dollars every quarter or in a year. It is important to note that the UN metric does not establish that IFFs as a yearly flow or a yearly average of a cumulative flow. The correct unit expression for financial flows should be "US dollars per year", not "current US dollars".

This incorrect conceptual designation of the relevant unit opens up the discussion for a stock variable, one which does not require a time-unit denominator. However, flows and stocks are not the same. In fact, in practice, many statisticians compile stock figures derived from cumulative flows. But flows do not exist in vacuum; they accumulate to form a stock figure, even if the stock figure is invisible.

An illicit financial stock or "illicit financial cumulative flow" (IFFC) of the South’s assets are liabilities of the North. According to Boyce and Ndikumana (2000), Africa’s external assets (many originated via IFFs) are larger than its official foreign debt, and thus, Africa is a net creditor. An IFCF would imply that there is debt—as measured by the broadest definition of debt in the Quarterly External Debt Statistics (QEDS)—owed by the economies of the North to the economies of the South. The loaded term "debt" carries with it an obligation—perhaps moral, in this case—of repaying that debt to the South, akin to international reparations. Or at least, of "netting" the North’s debt with the South’s official foreign debt.

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A target that aims for, say, halving the cumulative IFFs by 2030 would imply pro-active policies to return these assets to the South and have net negative South-North IFFs through 2030. A target that aims for halving the IFFs in the year 2030 would imply continuous flows to the North, but only at half the rate at which they were occurring, only in the year 2030 (i.e. no return). Using yearly flows only reduces the bleeding, it does not stop it. By using cumulative flows, we not only put a stop to the bleeding but actually recover the drained resources of countries of the Global South.

The elements discussed in this section are meant to raise several issues related to the interaction between the conceptual definition of IFFs and the relevant metrics around it. From here we move to understand a unifying approach towards addressing the retrogressive impact on the realisation of rights.
Why use a Human Rights Framework?

A human rights perspective provides an opportunity to move away from the “legal vs. illegal” narrative trap which restricts definitive action. The rights-based approach places scrutiny on not only how businesses, investors, elites and their enablers operate but also provides ways to assess the impact and intent of an “activity” based on existing human rights norms and standards.

Thus, the module proposes to view IFF as a cross-border financial flow arising from an illegal or abusive transaction in terms of its nature, origin, transfer, use or destination.

In March 2015, the interim study presented by the Independent Expert to the 28th session of the Human Rights Council highlighted the role of tax avoidance or minimisation practices signalling a major shift in how the issue has been framed so far. “(...) illicit financial flows encompass in addition to all kinds of artificial arrangements that have been put in place for the essential purpose of circumventing the law or its spirit, including certain legal “tax-optimization” schemes, making use of legal loopholes that allow for example transnational corporations to shift around profits to zero or low corporate tax jurisdictions, without undertaking any real economic activities in those jurisdictions.” Connecting tax abuse to human rights the Independent Expert argued that “tax abuse deprives Governments of resources required to progressively realize human rights, including economic, social and cultural rights, such as health, education, social protection, water, sanitation, as well as civil and political rights, including access to justice, free and fair elections, freedom of expression and personal security. Tax abuse can also undermine the rule of law, for example, when large-scale tax evasion is allowed to occur with impunity.” While listing recommendations for states, international bodies and non-state groups, the final study linked tax abuse with principles of equality and non-discrimination.

There are primarily two approaches that inform such a framing—one follows a transparency and accountability lens and the other being a “violations-based” approach. This is crucial especially in light of no legally binding charters with human rights agenda solely aimed at tackling IFFs. If the fight against illicit financial flows is rooted in the language and dynamics of human rights, including conventions like the International Covenant for Economic, Social and Cultural Rights, International Covenant on Civil and Political Rights, International Convention on the Elimination of all Forms of Racial Discrimination and their accountability mechanisms, it addresses the long-standing impediments and obstacles that are faced by human rights advocates and defenders seeking justice.
**Kathmandu Declaration’s typology of IFFs**

Illicit financial flows are generated from financial activities and practices that cause harm or that are illegal, and are abusive in their use of instruments and agreements in the international financial and economic system. These include issues such as tax abuse, abusive tax incentives, abusive use of bilateral or multilateral trade treaties, misuse of double tax treaties, odious debt, abusive use of mutual arbitration procedures, harmful tax practices, and unjust investment agreements, money laundering, trade misinvoicing, abusive transfer pricing, illicit money transfers, crime, bribery, illicit drug trade, corruption, and the ‘offshore’ trust industry.

- The Kathmandu Declaration on Curbing Illicit Financial Flows: Restoring Justice for Human Rights, 2018

The inclusion of the word ‘abusive’ in the definition draws emphasis on any intended or unintended harm caused in terms of the enjoyment or realisation of different human rights. It is preferable to use the term tax abuse, as it clearly attempts to define the purpose of any tax structure through motivation or primary usage. For example, even if nationally states are able to secure and safeguard their taxing rights through appropriate laws and rules. Multinational corporations (MNCs) and investors use international dispute settlement platforms to sue governments to reverse a regulation or recover any losses incurred due to compliance measures that have negative implications on investments. In March 2019, 7 UN independent experts sent a letter to the Working Group III on ISDS Reform highlighting the ISDS mechanism’s well-established incompatibility with international human rights law and asymmetrical system that encroaches upon the States’ fiscal space. Civil society too for long has advocated against how this characteristically undermines state sovereignty and threatens economic, social and civil rights. Not that all investor disputes will have components of tax abuse, the term still allows us to look at the spirit and impact of the financial flow as much as its legal status in any given jurisdiction.

The Kathmandu Declaration’s typology is also a huge step forward in describing the unequal economic and financial relations inherent in the current financial architecture and adequately reflects the evolution of the definition of illicit financial flows over time. It is not only a conceptual synthesis, but also a political recognition of the struggles by civil society and sovereignty-oriented Governments of the South.

Table 2 describes the main recent multilateral (or at least plurilateral) policy shifts or impacts related to the issues listed in the Kathmandu Declaration.
Why use a Human Rights Framework?

Harmful Tax Practices
Investigation and regulation of “Big 4” auditing companies

Unjust Investment Agreements
Reform of the ISDS regime at UNCITRAL and ICSID

Money Laundering and Terrorism
- FATF led reforms
- Regional financial intelligence units - Financial Task Force of Latin America (GAFILAT19), Asia Pacific Group on Money Laundering and Eastern and Southern Africa Anti-Money Laundering Group

Crime
- FATF led reforms
- UNTOC led reforms

Bribery
- FATF led reforms

Corruption
- UN Office for Drugs and Crime led reforms, Stolen Asset Recovery Initiative
- African Union Summit, UNECA

Illicit Money Transfers
- FATF led reforms, including on cryptocurrencies

Illicit Drug Trade
- FATF led reforms
- UNODC led reforms

‘Offshore’ Trust Industry
- Public registries in UK overseas territories
- Global Asset registry proposal

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Why use a Human Rights Framework?

Misuse of Double Tax Treaties
Limited reform of double tax treaties in light of information exchange conventions

Odious Debt
UN General Assembly resolutions and UNCTAD work on sovereign debt resolution

Abusive Use of Mutual Arbitration Procedures
Reform of the ISDS regime at UNCITRAL and ICSID

Trade Misinvoicing
- Unitary tax and formulaic apportionment of Transnational Corporations
- UNCTAD/UNECA/UNESCAP/UNECLAC/UNOSSC

Crime
- FATF led reforms

Bribery
- FATF led reforms

Corruption
- UN Office for Drugs and Crime led reforms, Stolen Asset Recovery Initiative
- African Union Summit, UNECA

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he Africa Process—The need for Africa to improve domestic resource mobilisation came at the backdrop of the Millennium Development Goals, and gave rise to an urgency to address the challenge of IFFs emerging from the region. It was in this context that a discussion to sensitise policymakers was initiated at the 4th Joint Annual Meetings of the African Union Commission (AUC)/United Nations Economic Commission for Africa (ECA) Conference of Ministers of Finance, Planning and Economic Development in March 2011.

The meeting was attended by representatives from 52 African countries, 20 UN Specialised agencies and 57 observer institutions including Bretton Wood institutions, other institutions from the Global North, International Non-Government Organisations and Africa based regional Non-Government Organisations such as the African Forum and Network on Debt and Development (AFRODAD), Coalition for Dialogue on Africa (CODA), African Capacity Building Foundation (ACBF) among others. After examining the issues at stake, participants called upon the UN Economic Commission for Africa (ECA) and the African Union Commission (AUC) to lead the efforts to combat IFFs from Africa. Consequently, the 4th Joint Annual Meetings of the AUC/ECA Conference of Ministers of Finance, Planning and Economic Development adopted a resolution mandating the establishment of a High-Level Panel (HLP) on Illicit Financial Flows from Africa and it inaugurated on 5th February, 2012 in Johannesburg, South Africa. Following the Resolution of the Ministers, the HLP had the primary role of further exploring and gaining a better understanding of the nature of illicit financial flows out of Africa and assessing its impact on the continent's development. In addition, it was envisaged that the HLP would work to increase collaboration and cooperation amongst African countries, their Regional Economic Communities and external development partners to promote a better global understanding of the scale of the problem for African economies and encourage the adoption of relevant national, regional and global policies, including safeguards and agreements to redress the situation.

The specific objectives of the HLP as derived from the Resolution were as follows:

- Determine the nature and patterns of illicit financial outflows;
- Establish the level of illicit financial outflows from Africa;
- Assess the complex and long-term implications of illicit financial flows on development;
-
Sensitise African governments, citizens and international development partners on the scale, and effect of financial outflows on development; and

Mobilise support for putting rules and regulations in place at all levels to tackle illicit financial outflows from Africa.

The Panel brought together eminent experts from within and outside Africa who shared common concerns around financing Africa’s development. It was chaired by H.E. Mr. Thabo Mbeki, the former President of South Africa while its Technical Committee was chaired by Dr. Abdalla Hamdok, the Deputy Executive Secretary of ECA. The HLP worked tirelessly with the support of its Technical Committee and through its Secretariat housed within the ECA in Addis Ababa playing an instrumental role in consensus building. The HLP report provided 15 recommendations to curb IFFs from Africa. Countries like Côte d’Ivoire, Ghana, Kenya, Niger and Senegal.

Stop the Bleeding Campaign

IFF Campaign aims to mobilize citizens across Africa towards galvanizing a broad support to tackle IFF including the implementation of HLP report recommendations. The launch of the Third International Conference on Financing Development was followed by national launches in Zambia, Togo and Nigeria.

The Cameroon Executive and Parliament endorsed the Stop the Bleeding campaign, the launch was covered by 5 local news channels depicting a vivid grassroots embrace of the campaign.

Ndèye Ndiaye, an alumni of the International Tax Justice Academy, is an active member of Citoyens Actifs pour la Justice Sociale. She collected 40 signatures through the STB website and physical signatures in Senegal. In addition, she attended a conference in Cameroon about governance of extractive industries where she planned to amplify the message on STB to collect more signatures.
Malawi, Nigeria, Sierra Leone and Tunisia have begun to implement policies on IFFs as per the recommendations of the report⁴³.

Gearing toward actions

Following the endorsement of the High-Level Panel (HLP) Report on Illicit Financial Flows (IFFs) from Africa and the passing of the AU Special Declaration by the African Union Heads of States at the 24th African Union Summit in 2015, there was an obvious need to implement its recommendations nationally, regionally and globally. Accordingly, a coalition of Stakeholders which became the Consortium of Stakeholders to Stem IFFs from Africa, was established⁴⁴. Above all else, the Consortium of stakeholders works to foster coherent implementation of the recommendations of the High-Level Panel and ultimately stem the growth of IFFs from Africa. The Consortium further constituted a core group within itself to address all technicalities with regards to implementing the recommendations of the High-Level Panel and ultimately stem the growth of IFFs from Africa. Specifically, the steps agreed upon include strengthening the institutional and regulatory capacity of African countries to combat illicit outflows, increasing advocacy for national and continental policy changes and establishing a multifaceted but united front to address the complex nature of illicit financial flows from the continent. CQDA which has been a key member of the anti-IFF working group and operates as a special initiative of the AUC, UNECA and African Development Bank, directly leading the administrative efforts of the implementation process. Last year, the Secretariat which was originally housed at ECA was moved to AUC to reinforce the monitoring of commitments made by the African Heads of State as per the HLP recommendations.

Simultaneously, the members of the anti-IFF working group have been working to follow-up on and implement the decisions of the Consortium and the Project using their collaborative capacities to do so. This includes the work of CoDA and Trust Africa on the current development of an IFF Knowledge Hub, a centralised source of information aimed at increasing awareness among policy makers and the general public, as well as the co-organization of a Meeting to Converge Civil Society and the Media by both institutions. As of June 2019, the consortium secretariat is committed to developing a knowledge hub on IFFs and ensuring that the yearly organisation of the Retreats of African Ambassadors to the UN and EU, to be led by AUC, begins from 2019 and involves selected members of the IWG.

Rising Above IFFs

Illicit money been laundered through shell entities by oligarchs, corporates and the far-right to subvert elections in several countries but also to routinely sway public, regionally towards anti-minority, xenophobic narratives through the spread of misinformation.

Putting an end to all kinds of illicit finance is an entry point towards reclaiming space in a democracy for ensuring accountability among state and non-state actors and redistributive politics which enables true public participation and representation. There is a need to go beyond and call out the continued operations of secrecy regimes that act as turntables for financial flows emerging from developing regions. But all of this begins with adopting a progressive and well-rounded definition of illicit financial flows that reflects the impact on human rights in developing countries.

In Table 3 on the next page, we provide a matrix of immediate and long-term approaches civil society actors can follow. We would strongly recommend going through the other modules to gauge how interventions can be suited to your context.
**Table x: Immediate and long-term approaches civil society actors can follow**

**Best Practices**

**Developing regions apart from Africa have been significantly influenced by the High-Level Panel report.**

- Using existing research and scoping on the Global South to build on evidence.
- Building awareness through various interventions
- Establish public registers of ultimate beneficial ownership. Countries like Kenya, Afghanistan, Jamaica have committed to public beneficial ownership registers.
- Regional tax forums to enable meaningful cooperation and participation on behalf of civil society organisations and journalists from the Global South can together track national or regional cases on economic regional bodies and its member states to undertake similar exercises to uncover different sources of illicit financial flows from their region.
- Civil society organisations and journalists can track national or regional cases on similar economic offenders across borders.

**Civic society organisations must advocate with UN regional economic bodies and its member states to undertake similar exercises to uncover different sources of illicit financial flows from their region.**

- Establish public registers of ultimate beneficial owners (true human owners) to challenge all forms of offenders across borders.
- Civil society organisations and journalists can together track national or regional cases on similar economic offenders across borders.

**Asia-Pacific civil society should advocate for a pan Pacific forum on tax under the auspices of UNESCAP to strengthen regional cooperation, similar to the African Tax Administrators Forum (in Africa) and Inter-American Center for Tax Administrations (in LAC).**

**End Notes**


2. Balance of payments are economic transactions of a country that take place in a specified period between that country and the rest of the world. These estimates were compiled by IMF which since 1950 have undergone several revisions.


7. As of October 2019, the definition and data in the SDG monitoring is yet to be defined. There is no certainty for the definition to come out by 2020 after. Despite demands in the FID process, to monitor and report back on progress on tackling IFFs by 2020, it has been unable to come up with a comprehensive definition.

8. For example, the US position on IFFs at the UN (Palermo, 2018). Available at: https://unresolutionmonitor.com/7569

9. A form of profit shifting where the money originating from the South is shifted abroad and “owned” by foreign nationals.


11. Unlike the Multilateral Convention for Administrative Cooperation on Tax Matters, the US has unilaterally directly acquired information from over 14,000 banks and financial institutions on the basis of unilateral legislation known as FATCA.
22. See here: http://codainaction.org/iff/


25. Building onto the work done by the HLP, the Interim Working Group (IWG) of the African IFF campaign platform comprising six Pan African organisations namely, Tax Justice Network Africa (TJNA), Third World Network Africa (TWAN-Africa), African Women’s Development and Communication Network (FEMNET), the African Regional Organisation of the International Trade Union Confederation (ITU-C-Africa), and Trust Africa supported and joined by the Global Alliance for Tax Justice launched a unified African campaign on IFFs dubbed “STOP THE BLEEDING” on June 2015 in Nairobi, Kenya.

26. A beneficial owner is a living person, who exercises economic control over an entity either directly or by using legal arrangements (i.e. indirectly) or accrues gains from transactions made under that entity. A public beneficial ownership register containing information on ownership structures and arrangements on all legal entities (companies, trusts, foundations, limited liability partnerships, associations, co-operative societies).

How to Use the Toolkit?

The toolkit is as an easy and accessible resource for enthusiasts, activists, civil society organisations, practitioners and journalists. Designed in a modular format, the toolkit aims to enable evidence based advocacy from the perspective of developing countries for bringing awareness, policy change, exchanging examples of effective interventions from the Global South and wider collaboration between different actors. Please note that the policy recommendations are aimed to be adapted and tailored across settings, regions and priorities.

All modules are designed independently from each other but are structured in a holistic manner. It is recommended that Module 1 be read first as it sets the premise for this undertaking. The toolkit fulfills three objectives -

- Provides a well-rounded perspective of illicit financial flows from the Global South context and delving into its regional components.
- Introduces terms that are set under the framework of human rights, gender justice and the sustainable development agenda with respect to redressing the impact of illicit financial flows.
- Uses a multi-pronged approach to involve the larger civil society, practitioners and journalists through international and regional mechanisms, simplified case studies to demystify complex topics and examples of successful interventions across the Global South.

The toolkit is available in print and online. The technical module is available in Spanish.

A Toolkit on Illicit Financial Flows: Perspectives from the South

Module 1: Politics of Defining IFFs
Module 2: IFFs and the Extractives Section in Asia
Module 3: Advocacy Manual for Lawyers’ Association in the Global South
Module 4: Addressing Illicit Financial Flows – National, Regional and Global Interventions
Module 5: Technical module: The Role of Banking in Latin America as a facilitator of Iff Financial Flows

This toolkit uses the term developing countries or regions interchangeably with the Global South. The term “Global South” represents countries in the developing regions of Africa, Asia and Latin America, Central America, Mexico, South America, and the Middle East (with the exception of Israel, Hong Kong, Macau, Singapore, South Korea, and Taiwan). Southern countries refer to countries belonging to the Global South.
About Financial Transparency Coalition
The Financial Transparency Coalition (FTC) is a global civil society network working to curtail illicit financial flows through the promotion of a transparent, accountable and sustainable financial system that works for everyone. For more information, kindly visit: https://financialtransparency.org/
Combating Illicit Financial Flows in the Extractives Sector in Asia
About the project:
For a unique space under the Financial Transparency Coalition (FTC), the Southern Regions Programme (SRP) plays a crucial role of an incubator by placing tax systems and financial transparency at the heart of development debates. In October 2017, during a South-South strategy meeting it was recognised to bring out a collaborative document that emerged from the perspective of the Global South. Five members1 of the SRP came together to author the IFF Toolkit in an effort to address issues of financial secrecy, enablers of illicit financial flows, lopsided impact on domestic resources and the ability to raise further resources due to loss of revenue as IFFs and the much-needed reforms in the international financial architecture set in the context of Global South. The toolkit uses case study-based evidence to simplify the issue of tax abuse. The document also covers tax incentive abuse as a subject under IFFs. The toolkit has benefitted from discussions held at the Nepal Social Forum (March 8th-10th, 2018), Paper on Illicit Financial Flows: Rights, Restoring Justice and Freedom and Pan-Continental Southern Dialogue on Illicit Financial Flows2, Nairobi (November 21-22, 2018).

Disclaimer:
The publication has been produced by the Asian People’s Movement on Debt and Development (APMDD) who is also a member of the Southern Regions Program in the Financial Transparency Coalition (FTC). This output does not intend to reflect the positions of all members of FTC.

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Author: Mae Buenaventura, expert inputs provided by Neeti Biyani

Designed by: How India Lives (www.howindialives.com)

For more information about the module, kindly write to: buenaventuram213@gmail.com

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1 Asian People’s Movement on Debt and Development (APMDD), Centre for Budget and Governance Accountability (CBGA), Latin American Network on Economic and Social Justice (LATINASOD), Pan African Lawyers Union (PALU) and Tax Justice Network Africa (TJNA)

A Toolkit on Illicit Financial Flows: Module II

List of Acronyms

AAAA — Addis Ababa Action Agenda
AE — Adaro Energy
AI — Adaro Indonesia
APAC — Asia and the Pacific
CCA — Coal Contract of Agreement
DTAA — Double Taxation Avoidance Agreement
EI — Extractive industries
EITI — Extractive Industries Transparency Initiative
FDI — Foreign direct investment
GDP — Gross domestic product
IASB — International Accounting Standards Board
IFFs — Illicit financial flows
IFRS — International Financial Reporting Standards
IMF — International Monetary Fund
NRC — Natural Resource Charter
NRGI — Natural Resource Governance Institute
PWYP — Publish What You Pay
TNCs — Transnational corporations
UNCAC — United Nations Convention Against Corruption
UNESCAP — United Nations Economic and Social Commission for Asia and the Pacific

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Extrative industries (EI) involve any process to extract raw material from the earth, most commonly oil, gas, metals and minerals. Oil, gas and mineral resource wealth is widespread in developing countries and often accounts for large shares of countries’ gross domestic product (GDP), export earnings, government revenue and jobs. It currently generates about $3.5 trillion in annual gross revenue throughout the world, which translates to roughly 5% of global GDP. However, evidence suggests a “resource curse” hounding mineral-rich countries who generally perform worse than their counterparts in economic terms. In this module, we look into some of the reasons behind this.

Perhaps, the most corrosive feature of EI is the fact that high economic rents which characterise this sector create room for illicit financial flows (IFFs)—this includes but is not limited to abusive transfer pricing, trade misinvoicing, tax abuse through corporate tax structures, corruption, misappropriation of state assets, etc. IFFs deprive countries, especially in the Global South, of crucial revenue that they deserve, thus inhibiting their ability to establish sound institutions, law enforcement processes and agencies as well as capacity within public bodies to check the various modalities of IFFs in the extractives sector.

1.1. Why is the extractive sector prone to IFFs?

First, there is a high degree of discretionary political control within the sector. Concentration of natural resources in certain geographical areas as well as their economic and revenue potential often leads to the extractives sector being controlled by the office of the head of the state and a few technocrats, with extremely opaque processes governing it. Further, the discretionary funds generated by the sector increases the autonomy of political leaders who control the governance of EI, thus reducing transparency and accountability and increasing resistance to reform.

Second, there is extremely limited competition in the extractives sector, resulting in fewer checks and
Combating Illicit Financial Flows in the Extractives Sector in Asia

A Toolkit on Illicit Financial Flows: Module II

Introduction and Background

Introduction and Background

Extractives Industries and Human Rights

While extractives industries are vital to the economy of several developing countries, companies in this sector are often accused of being involved in serious human rights abuses, including displacement of communities, environmental pollution and degradation, poisoning of land and water, denial of freedom of expression and association, child labour, and attacks on and killings of human rights defenders. There are different impacts on human rights along different phases of the value chain of extractives.

Perhaps the most systemic way in which EI impact human rights is by contributing to illicit finance across the world. IFFs have severe and differentiated impacts in countries in the Global South, which have inadequate funding for public services such as education, public hospitals, water and sanitation, public infrastructure, social protection and gender equality—all of which play a crucial role in the lives of the citizenry, especially marginalised communities. IFFs disproportionately impact women and their human rights, as they end up being taxed more and bear the brunt of inadequate public services.

balances compared to other more competitive sectors.

Third, the distinction between public, shareholder and private interests in the extractives sector is often blurred. State-owned companies may cater to the interests of their political patrons, while government officials may have vested financial interests in the sector. Public officials may also sit on the Board of Directors of private extractive companies, and thus have financial stakes in the profitability of these businesses.

Fourth, the extractives sector involves technical and financial processes that are complex, niche and require a great level of expertise. This sector is probably one of the very few in the entire world which is self-governed to a large extent, especially in developing countries. Instead of government agencies, companies carry out accounting for tax payments themselves. Thus, if auditing capacity is limited or corrupt, companies may engage in cost inflation, mispricing and manipulation—activities that are particularly harmful within the extractives sector, given the high reliance of countries on revenue from this sector.

High-level intergovernmental processes and initiatives too have drawn attention to opacity entrenched in the extractives sector, linking this with the sector’s potential for facilitating IFFs. The outcome document of the Third International Conference on Financing for Development, the Addis Ababa Action Agenda (AAAA) underscores as one of the action areas “the importance of corporate transparency and accountability of all companies, notably in the extractive industries.”

The report by the High-level Panel on Illicit Financial Flows from Africa (popularly referred to as the Mbeki Panel) also linked the extractives sector with IFFs, warning that “[c]ountries that are rich in natural resources and countries with inadequate or non-existent institutional architecture are the most at risk of falling victim to illicit financial flows”. It further observed that the extractives industry exercises a “high degree of discretionary power and political influence”.

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Combating Illicit Financial Flows in the Extractives Sector in Asia

Exploring the interlinkages between EI and IFFs becomes even more crucial given the sheer size of revenue, scale of operations and reach of Northern-based giant mining transnational corporations (TNCs) into richly mineralised but impoverished developing countries in Asia. APAC’s share of mineral and energy production rose from 33% of the global total to 48% between 2000 and 2015.7

Underscoring the need for a careful weighing of socio-economic costs and stricter regulation, the extractive sector’s contribution to GDP in a number of Asian countries often pales in stark contrast to the large profits gained by mining investors and the irreversible damage to the environment. In India, for instance, mining’s contribution to GDP has remained below 5% even after liberalisation, while small and medium enterprises contribute an estimated 29% with more employment generated and less harm to people and natural resources.8 The Philippines exhibit a similar situation; the sector contributed 0.85% in 2017 to GDP, with a slight rise from 0.79% in 2016.9

While taxation of natural resource extraction is a sovereign decision, mineral regimes interact with trade, investment, finance and international tax in a complex manner, leading to gaps and overlaps, and often weakens revenue collection.

2.1 Modalities of and risks involving illicit financial flows from the extractives sector

IFFs generated from the extractives sector can
be categorised into three sources, each from operations that reward different beneficiaries; sources that are not mutually exclusive but often go hand-in-hand. The first source consists of corruption, involving abuse of public authorities for personal interest. The second source consists of revenue from illegal resource exploitation in which the state does not receive its legal share. The third source is tax abuse by the companies in the extractives sector.

Further, the risk of illicit financial flows varies greatly across the different phases of mining activities. A study by the UN Economic Commission for Africa applying the extractive industry’s value-chain analysis to mining projects in several African countries illustrates this (see Table 2).

Table 1: Sources of illicit financial flows generated by the extractives sector

<table>
<thead>
<tr>
<th>Financial flows</th>
<th>Main beneficiaries</th>
<th>Corrupt government officials and companies gaining undue advantage</th>
<th>Domestic companies, local subsidiaries of foreign companies</th>
<th>Parent or holding companies, exporting companies</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Corruption</th>
<th>Illegal exploitation</th>
<th>Tax abuse</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bribe paid by companies, money embezzled from tax collection and budgetary allocations</td>
<td>Undeclared corporate revenues from illegal resource exploitation</td>
<td>Inflated costs deducted from taxable revenues, smuggling of resources</td>
</tr>
</tbody>
</table>

Source: Based on U-4 Anti-Corruption Resource Centre, 2011

Table 2: Modalities and risks involving illicit financial flows along the extractives value chain

<table>
<thead>
<tr>
<th>Licensing</th>
<th>Illegal Exploitation</th>
<th>Tax Abuse</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk Level: High</td>
<td>Key method: Bribery; commissions</td>
<td>Loopholes: Weak oversight institutions and weak accountability mechanisms</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>International Third Party Effects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk Level: Low</td>
</tr>
<tr>
<td>Loopholes: Unfair bidding &amp; award processes extortion</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Development</th>
<th>Illegal Exploitation</th>
<th>Tax Abuse</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk Level: High</td>
<td>Key method: Bribery, unlawful gifts and commissions</td>
<td></td>
</tr>
<tr>
<td>Loopholes: Non-compliance with contractual arrangements</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>International Third Party Effects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk Level: Low</td>
</tr>
<tr>
<td>Loopholes: Lack of enforcement of mineral sector regulations (e.g. procurement irregularities)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Exploration</th>
<th>Illegal Exploitation</th>
<th>Tax Abuse</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk Level: Low</td>
<td>Key method: Bribery, commissions</td>
<td></td>
</tr>
<tr>
<td>Loopholes: Non-compliance mechanisms; weak law &amp; order enabling trespassing beyond gazetted areas</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>International Third Party Effects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk Level: High</td>
</tr>
<tr>
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</tr>
</tbody>
</table>
**A Toolkit on Illicit Financial Flows: Module II**

**Combating Illicit Financial Flows in the Extractives Sector in Asia**

**Production**

**Illegal Exploitation**

- **Risk Level:** High
- **Key method:** Bribery; commissions; fraud
- **Loopholes:** Weak accountability mechanisms which enable underreporting and undervaluing of the minerals

**Tax Abuse**

- **Risk Level:** High
- **Key method:** Bribery; kick-backs; commissions; fraud
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for transfer mispricing; under-invoicing

**International Third Party Effects**

- **Risk Level:** Medium
- **Key method:** Bribery; kick-backs; commissions; fraud
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for transfer mispricing; under-invoicing

**Transport, storage and marketing**

**Illegal Exploitation**

- **Risk Level:** High
- **Key method:** Bribery; commissions; fraud
- **Loopholes:** Weak accountability & enforcement mechanisms; smuggling

**Tax Abuse**

- **Risk Level:** High
- **Key method:** Bribery; kick-backs; commissions; fraud
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for transfer mispricing; under-invoicing

**International Third Party Effects**

- **Risk Level:** Medium
- **Key method:** Bribery; kick-backs; commissions; fraud
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for transfer mispricing; under-invoicing

**Processing and marketing**

**Illegal Exploitation**

- **Risk Level:** High
- **Key method:** Bribery; commissions; fraud
- **Loopholes:** Weak accountability & enforcement mechanisms

**Tax Abuse**

- **Risk Level:** High
- **Key method:** Bribery; kick-backs; commissions; fraud
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for transfer mispricing; misinvoicing

**International Third Party Effects**

- **Risk Level:** High
- **Key method:** Bribery; racketeering; smuggling
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for transfer mispricing; under-invoicing

**Abandonment and decommissioning**

**Illegal Exploitation**

- **Risk Level:** Low, except for post decommissioning on illegal exploitation
- **Key method:** Bribery; commissions; fraud; racketeering; extortion; smuggling
- **Loopholes:** Weak enforcement mechanisms

**Tax Abuse**

- **Risk Level:** High, through early exit or fabricated bankruptcy
- **Key method:** Bribery; kick-backs; commissions; fraud
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for transfer mispricing; under-invoicing

**International Third Party Effects**

- **Risk Level:** Medium
- **Key method:** Bribery; kick-backs; commissions; fraud
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for transfer mispricing; under-invoicing

**Effects on budgetary allocation on mineral rich countries**

**Illegal Exploitation**

- **High impact**
- **Key method:** Money-laundering; smuggling
- **Loopholes:** Political instability; weak noncompliance mechanisms

**Tax Abuse**

- **Very High impact**
- **Key method:** Bribery; kick-backs; commissions; fraud
- **Loopholes:** Lack of enforcement of mineral sector regulations allowing for under-invoicing of imports

**International Third Party Effects**

- **Very High impact**
- **Key method:** Embezzlement; kickbacks; fraud; white-collar crime; insider-trader on commodity exchange markets
- **Loopholes:** Weak public financial management systems; weak oversight institutions; inadequate accountability mechanisms

**Source:** United Nations Economic Commission for Africa (2017)
While providing an overview, a caveat to reading Table 2 is that it significantly collapses the extractive process and does not allow interrogation of the defining factors before, after and in-between these discrete stages. Moreover, it is the extractive industry’s own value chain analysis, i.e., proceeding from the concern for commodities and their market value, competitive edge and opportunities for increasing business profits illustrating private sector interests based on profit maximisation. “This perspective... follows the commodity instead of the assets of the government,” notes the Natural Resource Governance Institute (NRGI). A more expansive approach proceeds from the responsibility of states to maximise value for their citizens, and the author’s attempt to highlight the possible loopholes for tax abuse and IFFs are shown in Table 3. This is an initial effort that invites further development based on different contexts.

Table 3. Value chain approach to natural resource wealth and peoples’ wellbeing

### Getting a fair deal

#### Features

- Defining a sustainable, climate-responsive and rights-based framework for awarding rights to explore and extract, and establishing the legal and financial terms governing those rights.

#### Some questions to plug loopholes for tax abuse and IFFs

- How were the terms negotiated?

### Country examples of issues

#### IFFs arising from illegal activity:

**Indonesia:** Due to overlapping regulations and the licensing system, between local governments, ministries of Energy, Forestry and Natural Resources resulting in illegal contract awards (e.g., open pit mining in conservation forests protected from any extractive activity).

#### Disadvantageous mining tenurial arrangements (favoring corporations):

**Philippines:** Under the Financial and Technical Assistance Agreement (FTAA), the State only gets the share provided for by law only after the contractor has fully recovered its pre-operating, exploration and development expenditures, whenever that may be since there are no time prescription. Furthermore, this share is defined as consisting of taxes, fees and duties. Additional share (on top of taxes, etc.) from profits may never be reached because of unrealistic conditions. These include the proviso in the implementing rules that the investor will only give an additional “share” only if net, after-tax income exceeds 40% of gross output for two consecutive years. Data covering nine years before 2011 showed that the highest net income after tax/gross output ratio was only 25%, with the average ratio at 16% over a nine-year period.

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### Arriving at the decision to extract

#### Features

- Defining the extraction framework.
- What is value/valueable to people and the environment, and value creation?

#### Some questions to plug loopholes for tax abuse and IFFs

- How were the licenses obtained and contracts awarded?
- Are there overlapping, conflicting laws and policies?
- Were “politically exposed persons” involved?
- Were the affected communities adequately and meaningfully consulted; Was free, prior and informed consent secured?
- How were social and environmental safeguards complied with? Is the identity of the beneficial owners disclosed?

### Country examples of issues

#### IFFs arising from illegal activity:

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#### Disadvantageous mining tenurial arrangements (favoring corporations):

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While providing an overview, a caveat to reading Table 2 is that it significantly collapses the extractive process and does not allow interrogation of the defining factors before, after and in-between these discrete stages. Moreover, it is the extractive industry’s own value chain analysis, i.e., proceeding from the concern for commodities and their market value, competitive edge and opportunities for increasing business profits illustrating private sector interests based on profit maximisation. “This perspective... follows the commodity instead of the assets of the government,” notes the Natural Resource Governance Institute (NRGI). A more expansive approach proceeds from the responsibility of states to maximise value for their citizens, and the author’s attempt to highlight the possible loopholes for tax abuse and IFFs are shown in Table 3. This is an initial effort that invites further development based on different contexts.

### Arriving at the decision to extract

#### Features

- Defining the extraction framework.
- What is value/valueable to people and the environment, and value creation?

#### Some questions to plug loopholes for tax abuse and IFFs

- How were the licenses obtained and contracts awarded?
- Are there overlapping, conflicting laws and policies?
- Were “politically exposed persons” involved?
- Were the affected communities adequately and meaningfully consulted; Was free, prior and informed consent secured?
- How were social and environmental safeguards complied with? Is the identity of the beneficial owners disclosed?

### Country examples of issues

#### IFFs arising from illegal activity:

**Indonesia:** Due to overlapping regulations and the licensing system, between local governments, ministries of Energy, Forestry and Natural Resources resulting in illegal contract awards (e.g., open pit mining in conservation forests protected from any extractive activity).

#### Disadvantageous mining tenurial arrangements (favoring corporations):

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Ensuring transparency in revenue payments

Features
Ensuring the collection of all kinds of payments, as spelled out in the extraction contract and the legal framework.

Some questions to plug loopholes for tax abuse and IFFs
- What cross-border transactions are involved?
- Are fees payments and revenues regularly published?
- Are revenues foregone from tax incentives weighed against actual payments?
- Is information publicly accessible (including language), unconditionally available and comprehensive? Are these subjected to independent, credible and participatory audits, and reconciled by equally credible, independent administrators? Is civil society actively engaged?

Country examples of issues
Inadequacy, inaccessibility of information:
Cambodia: Bidding procedures have not been publicly announced, nor has the actual bidding process been announced. There is even less information on the resource revenues. Information available from the Budget ministry is not disaggregated into the different fees and taxes in the extractives sector. Other sector fees such as from licensing are also lumped under domestic licensing.

A 2011 mapping of information availability in connection with oil and gas deposits found on Cambodian territory found no publicly available data on draft laws and regulations (new petroleum law, taxation of oil operation, taxation of mines; expected areas of exploration/ extraction; bidding procedure for oil and mining; licensing fees for oil and gas operations).

Managing resource revenues

Features
Fiscal management: disposition of revenues;

addressing the issue of fluid commodity markets and the risk of dependency; safeguarding against corruption

Some questions to plug loopholes for tax abuse and IFFs
- Are revenues equitably and sustainably distributed and used?
- Are affected people and communities prioritised?
- Are mechanisms adequate for transparency and accountability and against corruption, and are sanctions clearly defined?
- What are the safeguards against commodity swings? Is public spending decoupled from resource revenues (i.e., with funding from stable revenue sources)?

Country examples of issues
IFFs arising from contexts where states are captured by elite interests:
“Myanmar’s jade licensing system is wide open to corruption andcronyism. The main concessions are in government-controlled areas of Hpakant Township, Kachin State, and blocks are awarded through a centrally-controlled process which multiple industry sources say favours companies connected to powerful figures and high-ranking officials.”

Investing for sustainable development

Features
Requiring systematic, sustained and periodic monitoring and evaluation; transparent and participatory audits of public expenditures.

Some questions to plug loopholes for tax abuse and IFFs
- Is revenue use in line with the human rights obligations and sustainable development agenda?
- How are the needs and interests of excluded, marginalised and vulnerable groups prioritised?

Country examples of issues
Myanmar:
Global Witness estimated the value of jade production at $31 billion in 2014 alone, a figure that is 46 times bigger than government’s public health spending."

*Note: This table is heavily informed by NRGI’s publication on “The Value Chain”.

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Indicators of Abuse in Extractive Industries

3.1 Tax abuse

There are various, though not exhaustive, indicators for detection of tax abuse by companies in the extractives sector. Such indicators can be used as early warning signs or detection tools for law enforcement agencies to strengthen the fight against such tax abuse. Most of these indicators must be considered in a specific context and in relation with other indicators. They often vary on a case-by-case basis. These indicators should raise concerns over the possible avenues for tax avoidance and motivate further investigation.

International offshore corporate structures that abuse national and international tax laws, especially those that have offshore entities within corporate structures located in low tax or secrecy jurisdictions are a useful starting point. Offshore companies incorporated in tax havens are frequently used or abused for tax avoidance and as a tool to commit various financial crimes. Further, a shareholder of a company can also be located in a tax haven. Trust or corporate service providers—along with offshore law firms, banks and accountancy firms—provide services such as acting directors or granting domicile, thus masking the true owners of the company.

Manipulating and misreporting volume or value of commodities and trade flows involve under- or over-valuing the prices of exported minerals to shift profits within the corporate structure of the mining company, known as abusive transfer pricing. Oil, gas and mineral reserves can also be under-valued at the exploration phase, or production values or the quality of extracted resources could be misreported to avoid various different types of taxes, including corporate tax and capital gains tax.

Financial statements, payments and financial flows form important indicators regarding the prevalence of abusive tax practices by mining companies.
companies. Intellectual property rights such as patents and trademarks are often placed in related entities incorporated in low-tax jurisdictions, enabling local mining companies to transfer considerable volumes of royalties to such entities and engage in profit shifting. Intra-group loans between different entities belonging to the same corporate structure may be used to shift costs from high tax to low tax jurisdictions. Thin capitalisation may also be applied, implying that the local mining company is financed with relatively more debt and less equity than is common in business practices. Further, dividend payments from the local mining companies to the parent company could be redirected via entities registered in secrecy jurisdictions instead of following hierarchical lines, resulting in tax abuse. Local mining companies could also under-report profits by accelerating depreciation of its assets—taxing deduction for the cost of the asset can reduce taxable income. Lastly, the absence of reporting operations, profits and payable taxes by companies on a country-by-country basis can also be considered an indicator for tax abuse.

While the tax base being lowered through various methods discussed above is a sound indicator, tax payments can also be abused. Companies could increase their reported income to shareholders, legitimately or illegitimately, while reporting lower profits to the country’s tax revenue authorities, indicating tax abuse. Bilateral tax treaties between a country where mining operations are carried out and the country where the parent entity is registered could also aid in lowering the tax burden. In some cases, an intermediate holding company can be incorporated in a third country with whom the parent company’s host country has a bilateral tax treaty. Though such arrangements are often cited for reasons of “tax planning” or “tax efficiency” by parent mining companies in their annual reports, these arrangements are ultimately abusive of national tax structures. Mining groups can further seek an advance tax ruling from the revenue authority of the country where the resource extraction is going to take place, most often due to power imbalances and asymmetric information.

3.2 Trade misinvoicing

Trade misinvoicing is a method for moving money illicitly across borders which involves the deliberate falsification of the value, volume, and/or type of commodity in an international commercial transaction of goods and services by at least one party to the transaction. By fraudulently manipulating the price, quantity, or quality of a good or service on an invoice submitted to customs, criminals can easily and quickly shift substantial sums of money across international borders.

In the extractive sector it is one of the largest drivers behind large volumes of IFFs, arising from massive illegal mining and the export of mining commodities which go largely unrecorded. For example, in Indonesia’s case, for instance, IFFs swelled considerably between 2003 and 2014 in the oil, gas, mineral and coal sectors at twice the national growth rate. In only a decade, IFFs rose from IDR 11.80 trillion in 2003 to IDR 23.89 trillion in 2014. This accounted for about $2 billion or over 10% of total IFFs from Indonesia in 2014. Large discrepancies have also been found between the data reported in South Africa’s custom data and the data reported by its trading partners—between 2000 and 2010, South Africa’s data shows $2.8 billion and $2.3 billion of exports under the head “non-monetary gold” in two different datasets, while its trading partners report $59.7 billion of non-monitored gold exported from South Africa. During the same period, under-invoicing of iron ore exports from South Africa to China was worth $3 billion.

While all data discrepancies are not necessarily IFFs, unrecorded trade transactions are prevalent and provide channels for moving illicit finance across borders, warranting a close watch to assess for fraudulent trade behaviour and tax abuse.

3.3 Transfer pricing abuse

Transfer pricing is the rule or method of pricing transactions between two companies that are part of the same transnational company group. For example, when a Nepalese subsidiary transacts with a Vietnamese subsidiary belonging to the same parent entity, the price of that transaction is known as the transfer price. However, for the transfer price to be legitimate, it should be comparable to the price of a transaction between unrelated entities (known as market price) which is informed by the “arm’s-length principle.”

Transfer pricing is one of the most fundamental building blocks of the current international accounting and tax system. While transfer pricing is not, in itself, illegal or necessarily abusive, two related companies trading with one another may artificially distort the price at which trade is recorded for minimising their tax bill. Transfer pricing manipulation or abuse is common and rampant and is one of the primary drivers of IFFs. EIs have a long and complex value chain, involving
Case study: Dirty money flows from dirty coal

The Jakarta-based firm Adaro Energy (AE) has swiftly grown into one of the largest producers of thermal coal in Indonesia and South-East Asia. By 2017, it declared a net profit of more than US$480 million, surpassing Indonesia’s largest coal producer. In 2018, AE’s revenues leaped up to US$3.6 billion. AE’s Chinese partner, Power Jiaxiang, is AE’s second largest mining company, operating Indonesia’s single largest coalmine under a 30-year Coal Contract of Agreement (CCA). Awarded in 1982, the CCA targeted investors for Indonesia’s still fledgling coal industry, with an incentive that protected early investors against any changes in Indonesian tax and investment laws. The CCA program underwent changes in later years to favour fully owned domestic players, but the first CCA holders such as Adaro maintained a greater advantage.

At one point, the Indonesian Finance Ministry brought in new rules that disallowed coal producers to deduct input VAT from output VAT; and removed the VAT exemption on materials and equipment. When questioned for offsetting claims for recoverable VAT against royalty payments, AI cited CCA terms that, “the Government will pay, assume and hold Adaro harmless from all Indonesian taxes, duties, rentals and royalties levied by the Government imposed after the date of the CCA.” The Supreme Court eventually ruled in 2017 that while AI had to settle the unpaid royalties, it will be refunded for VAT payments made after coal production became VAT-exempt in 2000.

Further, warning signs of profit-shifting through tax avoidance schemes is clearly illustrated by Al’s dealings with its Singapore-based holding firm, Coaltrade Services International Pvt. Ltd. Indonesian revenue officials found out that Coaltrade had bought coal from AI at US$32/tonne and subsequently sold it to third parties when prices rose to US$39/tonne. The parties were then booked in Singapore and taxed at only 10.7% (as compared to Indonesia’s 50.8%). The company later agreed to settle the dispute by paying US$3.2 million to the government.

For almost a decade, Coaltrade sourced more than 70% of the coal it was selling, from Adaro subsidiaries in Indonesia. Global Witness estimated that between 2009 and 2017, Indonesia had forgone corporate taxes of US$125 million or US$14 million/year. Meanwhile, Coaltrade enjoyed a spike in commissions from an annual average of $4 million to almost $55 million during the period. Adaro Indonesia holds a “Golden Taxpayer Status” from the tax authorities, ruling in 2017 that while AI had to settle the unpaid royalty payments due under the CCA. The Supreme Court eventually ruled in 2017 that while AI had to settle the unpaid royalties, it will be refunded for VAT payments made after coal production became VAT-exempt in 2000.

Transfer pricing abuse also manifests in the ways that corporations raise financing, especially when this is done through intra-group lending. Also referred to as debt shifting, the practice of price setting of intra-group transactions, discussed in the previous case study, illustrate transfer pricing abuse in the extractives sector, and reveal how setting the price may be a tax planning policy rather than arm’s length pricing.

3.4 Tax treaty shopping

The international tax system dates back to the early 20th century, when most businesses and corporations were national, international economic flows primarily consisted of trade and portfolio investment, and multinational corporations (MNCs) were in their infancy. The tax system was therefore shaped by domestic tax laws from that period and Double Taxation Avoidance Agreements (given business motivation to avoid being taxed twice). Informally called bilateral tax treaties, DTAs now number 3,000-4,000 across the world.

Most countries sign DTAs or bilateral tax treaties with the ambition of attracting investment, but evidence remains inconclusive on this. Numerous possibilities exist. The tax treaties further complicate this problem of revenue erosion in developing countries hosting extractive activities. Asian countries such as Cambodia, India, Indonesia, Lao PDR, Myanmar, the Philippines and Thailand do not have rules that guard against excessive debt and interest deductioms; or subject the debt to equity ratio to certain conditions as those provided by tax incentives and tax treaties.
A majority of DTAAs are signed between a developed and a developing country, and are restrictive on the rights of the source country to tax global corporations as they (i) place restrictions on the tax rate of income earned in the source country, including a cap on withholding taxes for dividends, interest payments, royalties and fees for management, and technical and paid to residents of the contracting states; (ii) set limitations on what can be taxed (e.g., definition of what constitutes a permanent establishment), which would otherwise trigger tax obligations under domestic law; and (iii) exempt other types of income (e.g., capital gains) earned in the source country from incurring taxes in that jurisdiction.

A pertinent example in this case would be Mongolia’s tax treaty with the Netherlands. The Oyu Tolgoi mine, an open pit and underground mining project in the southern part of the Gobi region has one of the largest gold and copper deposits in the world and is currently operated by the global mining group, Rio Tinto. In 2009, Rio Tinto’s Canadian subsidiary Ivanhoe Mines (now Turquoise Hill Resources) transferred a large part of its shares in the copper mine project to a Dutch entity. This resulted in freeing Rio Tinto’s Mongolian subsidiary from either the 10% withholding tax in the original investment agreement or the 5% withholding tax under the Mongolia-Canada tax treaty, and totally exempting it under the Mongolia-Netherlands treaty.

The Mongolian government informed the Netherlands in 2011 that it wanted changes in their tax treaty, but the latter refused. Later that year, the Netherlands conceded only one amendment—allowing a 5% tax on dividends. This was far below the 20% withholding tax Mongolia usually levied on dividends paid out by mining firms. Mongolia cancelled the tax treaty with the Netherlands in September 2012. Unfortunately, Mongolia had already agreed to ‘stabilising’ or freezing the terms of the original agreement. As a result, withholding taxes were lowered from 20%, then 10% and finally 6.6%, resulting in a reduction of Rio Tinto’s tax obligations by $232 million.

Unlike Mongolia’s decision of cancelling its tax treaty with the Netherlands, India renegotiated its tax treaty with Mauritius for nearly a decade. Signed in the early 1980s, the treaty provided for Mauritius-registered firms acquiring shares in India-based firms to pay capital gains tax on the sale of these shares only in Mauritius. However, Mauritius did not levy capital gains tax. In effect therefore, the tax treaty, meant to prevent being doubly taxed on the same economic activity, resulted in double non-taxation. The renegotiated 2016 Protocol made the important change of allowing India as the source jurisdiction to levy taxes on the transfer of securities to Mauritius-domiciled entities starting April 2017.

Tax treaty shopping (or treaty shopping) leads to substantial tax abuse by TNCs, aided by differences in withholding tax rates of thousands of bilateral tax treaties throughout the world. MNCs match tax treaties from which tax treaty benefits can be claimed by coursing FDI or dividend payments through countries with the lowest withholding tax rate. Studies have also established links between low withholding tax rates and the diversion of foreign investments by MNCs through third-party countries; a direct route between treaty partners would otherwise have been less profitable.

3.5 Liberalised investments and incentives regimes

A substantial number of Asian countries’ increasingly aggressive corporate tax incentives regimes have given way to intense tax competition between these states, resulting in a ‘race to the bottom’ to attract the most investment by offering lowest possible tax rates to investors and businesses. Despite states recognising the impact on revenue tax incentives have, they continue to offer them.

![Figure 1: Low-income Asian countries with the highest number of restrictive treaties](source: ActionAid (2016))
Indicators of abuse in extractive industries

This proliferation of tax incentives regimes provides a virtual roadmap for shifting profits to the lowest tax jurisdictions. The corporate tax base of a country can be eroded significantly by income shifting schemes employed by TNCs. Besides the production location, TNCs have an opportunity to choose the location of profit too, and exploit and gaps and loopholes in national and international tax law to shift profits to low tax jurisdictions. Facing different statutory tax rates in the jurisdictions where they have operations, they have an incentive to use transfer pricing to concentrate expenses in the country with the higher tax rate and income in the country with the lower tax rate. This type of income shifting typically occurs after they take full advantage of tax allowances available in a jurisdiction where they have an operation.29

Eligibility requirements, calculations, rates, instruments, etc. vary at national and sub-national levels across countries but both profit-based and cost or productivity-based incentives are commonly offered across Asian countries. Lowering corporate income tax rates has also grown into an established trend (see Figure 2).

Corporate income taxes remain a significant source of revenues for developing countries. Since the value of income tax holidays is proportionate to the reported profits earned, they benefit the biggest corporations that, in the first place, need the least amount of state support. These include mining TNCs that do not need tax incentives as they are established, highly profitable enterprises, but end up receiving incentives plainly because of the resource-seeking and location-specific nature of their business.

The role of government, regulatory reform and transparency initiatives

Several initiatives have been developed to improve transparency, accountability and governance of the extractives sector. Many of them have come into existence through the push of developed countries and international financial institutions and without benefit of public perusal and consultation, especially with extractives-affected communities.

![Figure 2: Average Corporate Income Tax Rates by the Decade](image-url)

Source: Tax Foundation (2018)
Engaging Initiatives for Transparency and Accountability in the Extractives Sector

In the growing pressure to curb illicit financial flows, transparency and accountability have become widely recognised by states, multilateral bodies and international institutions as requisites for building and defending public financial resources. The extractives industry in particular has come under closer scrutiny over the last two decades on transparency and accountability. It involves large capital investments by global transnational firms in resource-rich developing countries where large segments of the population also remain persistently impoverished. Many of these countries also lack infrastructure for adequate public provision of basic social services, thus raising governance questions over mining investments.

Examples of initiatives and mechanisms engaged by civil society to bring transparency standards to bear on the extractives sector are listed in this section. The EITI, for one, has helped provide information on corporate revenue payments to the public at large, and normatively, bound questions of transparency with the extractives sector. The need remains though, for critical study of strategies and programmes, greater efforts in consulting civil society, especially affected communities and excluded marginalised groups, and undertaking informed, participatory processes to ensure the effectiveness and responsiveness of initiatives.

Extractive Industries Transparency Initiative

**Brief Description**

This multistakeholder association of corporations, states and civil society is organised under Norwegian law and defines itself as "the global standard for the good governance of oil, gas and mineral resources". It advocates the open and accountable management of these extractives sub-sectors "based on the principle that a country’s natural resources belong to its citizens".34

**Entry points for CSOs**

The EITI standard is implemented through multistakeholder groups (MSGs) at the national level, formed at the lead of government after it commits to sign up to the process. Composed of the mining sector, government and civil society, the MSGs work out reporting guidelines, seek disclosure of payments and revenues, examine discrepancies, and ensure that information is disseminated.

The EITI agreed in 2016 on including in the standard, the requirement to disclose the ultimate beneficial owners should by January 1, 2020. Progress is being monitored and evaluated on whether extractive firms are providing information on the name, nationality and country of residence on the name, nationality and country of residence.
of the beneficial owner, and also identifying involvement by “politically exposed persons”.

Possible Drawbacks
Organisationally, as a voluntary initiative, it does not cover all extractive firms. These covered are not required to disclose their payments openly, but only to country members of EITI. This is problematic for regions like Latin America with only two members (Peru and Argentina), and Asia with four members (Philippines, Mongolia, Myanmar and Timor-Leste).

The US withdrew from the EITI in 2017 citing legal impediments. But this has been challenged by civil society; corporations’ resistance to disclose revenue payments is alleged as the main impediment to EITI implementation.

Other concerns point to the lack of tighter requirements to compel states to disclose how revenues from the extractives sector will be spent.

The focus on transparency while important is not sufficient to hold states and corporations accountable, and weed out corruption. Transparency mechanisms will only work where there is public awareness, committed and organised actions and an independent media.

Natural Resource Governance Institute (NRGI)
Brief Description
NRGI was set up in 2013 from the joining of two initiatives, the National Resource Charter and the Resource Watch Institute. Its goal is to “to help countries manage their natural resources for the public good by leveraging our expertise working with civil society, parliaments, governments, the private sector, media and other partners”.

Approaches include research and data analysis, developing policy advice and capacity development. It also has country presence in select countries where it looks at country needs and demand and relates this to aspects of the natural resource decision chain.

Entry points for CSOs
NRGI works in partnership with citizens, governments, and other actors in these areas: development of mechanisms for transparency and oversight; strengthening fiscal systems and contracts; reforming state-owned enterprises; and management of resource revenues.

Resource governance encompasses “the rules, disclosures, oversight procedures and enabling environment that allow citizens to hold their government to account for managing their extractive resource wealth”.

To assess these, the NRGI has developed the Natural Resource Governance Index, reported as the only comprehensive international index dedicated to measuring the quality of governance in the oil, gas and mining sectors of 81 countries. These include Bangladesh, Cambodia, India, Indonesia, Lao PDR, Malaysia, Mongolia, Myanmar, Timor Leste and Vietnam.

Possible Drawbacks
On indexes in general, summary data is important to guide policy makers, and inform civil society advocacy efforts. But there are also debates concerning the sources and quality of data (reliability and adequacy), lack of transparency and consultation, comparability, the absence of gender indicators, etc. The launch of the African Peer Review Mechanism—a governance tool—is one example of moves towards developing more in-country and/or region-led initiatives.

Civil Society Led Initiative
Publish What You Pay (PWYP)
Brief Description
PWYP is both a campaign for transparent, accountable extractive industry, and a global movement seeking to ensure that revenues from oil, gas and mining drive development. From its beginnings in 2002, it reports a 700 member-network that includes human rights, development, environmental and faith-based groups.

Entry points for CSOs
The PWYP Strategy for 2020-2025 rallies to a vision of a “people-centred agenda for the extractive sector”, which entails “pushing for governments to regulate natural resource extraction in an open and accountable way, for companies to operate within an effective governance framework, and for a civil society with the skills and freedom to drive natural resource extraction that benefits all”.

Strategic goals include promoting knowledge across its membership, building knowledge through research, advocacy and linking with other movements (e.g., climate, gender and tax justice movements).

Data Extractors Program—an ongoing global initiative that trains participants in uncovering extractives data, specifically to “expose discrepancies in company and government reports and payments to reveal corrupt practices with the ultimate goal of reversing the resource curse”.

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Illicit flows from EI are massive and are closely connected with governance and developmental issues. One of the immediate challenges is to connect the dots between agendas and movements, such as those around the sustainable management of natural resources; the equitable use of resource wealth, human rights, gender equality, and tax and fiscal justice. In the face of significant challenges, participatory and multi-pronged approaches are critical to synergise the efforts of policy-makers, civil society organizations, social movements and multilateral platforms to curb and eventually put an end to IFFs.

For civil society, steps towards curbing opportunities for IFFs in extractives should include –

- Conducting an independent citizens’ review of the preferential tax treatment in the extractives industry and their economic, social, environmental and fiscal justice impacts.
- Developing the principles for the comprehensive reform of the fiscal regimes governing the extractive industry.
- Raising capacity on understanding and monitoring the mechanisms and strategies for IFFs especially tax avoidance schemes utilized by extractives firms.

For policy-makers, it is important to develop a keen sense where and how IFFs may occur in the extractives industry. It is thus urged that more concerted efforts be made towards –

Enhancing transparency and accountability

Transparency and accountability should be extended along all phases of extractives activities,
within and across national borders, from pre-bidding conditions, licensing and awarding of contracts, and actual exploration and production processes, to mine closures, rehabilitation and payment of compensatory damages. Risks of IFFs can be identified and independently assessed if laws, implementing regulations, contracts and other vital information are made publicly available. Beneficial ownership, asset ownership and other registers should be publicly accessible for scrutiny in all jurisdictions.

There is a need to make transparency disclosures mandatory. Greater transparency in markets, especially on resource prices, also has the potential for reducing IFFs as well as reducing price volatility. Country-by-country reporting with lower public thresholds needs to be made mandatory for companies involved at the various stages of the extractives value chain.

Physical audits of illicit material flows should be made mandatory to assess if volumes of production and export are reliably measured and officially reported.

Customs agencies should treat trade transactions involving tax havens or secrecy jurisdictions with the highest level of scrutiny and request additional due diligence.

Addressing corruption and tax abuse

While countries are now obligated to enforce stricter standards against corrupt practices due to the United Nations Convention Against Corruption (UNCAC), they are less concerned about their extraterritorial responsibilities especially with regard to the activities of their companies overseas. States, as members of international human rights organisations have obligations relating to acts and omissions, within or beyond its territory, that have effects on the enjoyment of human rights outside of that State’s territory.

Business groups in the extractives sector which have subsidiaries registered in or routing profits through low-tax and secrecy jurisdictions present significant challenges to tax authorities. This requires multilateral engagement and cooperation on tax matters in a platform where developing countries are on an equal footing.

Weeding out opportunities for corporate tax abuse and IFFs in the extractives sector is part of bigger and long-standing struggles and movements for tax and fiscal justice. Supporting these cross-cutting demands thus works to advance efforts to curb IFFs in the extractives industry.

Global inequalities in taxing rights provide favorable environments for MNCs to engage in profit-shifting schemes, at the expense of countries in great need of public revenue. An intergovernmental body under the auspices of the UN and a legally binding UN Tax Convention offer ways forward. For both measures to be realised, critical mass and political will are key elements.

Allocate financial and technical resources to strengthen capacity of tax administrations especially in developing countries hosting large mining investments.

Put in place or enforce mechanisms for the public disclosure of the beneficial, or actual, owners of companies.

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Put in place or enforce mechanisms for the public disclosure of the beneficial, or actual, owners of companies.

Require public country-by-country reporting from multinational corporations operating and/or registered in their jurisdictions to report on their global commercial activities, structures and tax payments.

Support the call for the automatic exchange of tax information, with the objective of shining a light on illicit finance, their channels and enablers, including tax havens and freezing up these resources that could go into SDG implementation and the enjoyment of human rights. Developing countries require time and finance to capacitate their tax administrations; and until such time, it is only fair that reciprocity is not imposed as a condition in information exchange.
End Notes


3 For a detailed discussion on the subject of illicit financial flows, please refer to Module 1 of this toolkit.


7 UNDP and UN Environment (2017). Sustainable Development: A Sourcebook


10 Tax havens and secrecy jurisdictions are countries or even regions within countries that provide an escape from tax, tightly linked financial secrecy and a complete avoidance of criminal laws and regulations.

11 Beneficial owners are true human owners, who either directly or indirectly profit from and/or control assets and/or economic benefits in a company.

12 Tax capitalisation refers to the ratio of debt to equity.


16 Source country is one where economic activity actually takes place, and the OECD core important differences in the definition of ‘source’ country. A country need not be the permanent establishment of the taxpayer to be the source country, and it must be more clearly defined, that benefiting the investment-revenue country in terms of the tax revenues it can collect.

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26 Source country is one where economic activity actually takes place, and the OECD core important differences in the definition of ‘source’ country. A country need not be the permanent establishment of the taxpayer to be the source country, and it must be more clearly defined, that benefiting the investment-revenue country in terms of the tax revenues it can collect.

27 For a detailed discussion on the subject of illicit financial flows, please refer to Module 1 of this toolkit.


29 The provision on “Permanent Establishment” (PE) in tax treaties, spells out the various conditions by which a foreign corporation/ taxpayer becomes subject to tax obligations in the source country. The wording of such rules thus provide various levels of flexibility in situations such as those that may arise in the case of offshore corporations/taxpayers in tax havens. The OECD call for important differences in the definition of ‘source’ country. A country need not be the permanent establishment of the taxpayer to be the source country, and it must be more clearly defined, that benefiting the investment-revenue country in terms of the tax revenues it can collect.


31 United Nations Economic and Social Commission for Asia and the Pacific (2017). Tax incentives and Tax Base Protection in Developing Countries


How to Use the Toolkit?

The toolkit is as an easy and accessible resource for enthusiasts, activists, civil society organisations, practitioners and journalists. Designed in a modular format, the toolkit aims to enable evidence based advocacy from the perspective of developing countries for bringing awareness, policy change, exchanging examples of effective interventions from the Global South and wider collaboration between different actors. Please note that the policy recommendations are aimed to be adapted and tailored across settings, regions and priorities.

All modules are designed independently from each other but are structured in a holistic manner. It is recommended that Module 1 be read first as it sets the premise for this undertaking. The toolkit fulfills three objectives -

- Provides a well-rounded perspective of illicit financial flows from the Global South context and delving into its regional components.
- Introduces terms that are set under the framework of human rights, gender justice and the sustainable development agenda with respect to redressing the impact of illicit financial flows.
- Uses a multi-pronged approach to involve the larger civil society, practitioners and journalists through international and regional mechanisms, simplified case studies to demystify complex topics and examples of successful interventions across the Global South.

The toolkit is available in print and online. The technical module is available in Spanish.

A Toolkit on Illicit Financial Flows: Perspectives from the South

Module 1: Politics of Defining IFFs
Module 2: IFFs and the Extractives Section in Asia
Module 3: Advocacy Manual for Lawyers’ Association in the Global South
Module 4: Addressing Illicit Financial Flows – National, Regional and Global Interventions
Module 5: Technical module: The Role of Banking in Latin America as a facilitator of Illicit Financial Flows

The toolkit uses the term developing countries or region interchangeably with the Global South. The term “Global South” represents countries in the developing regions of Africa, Asia and Latin America, Central America, Mexico, South America, and the Middle East (with the exception of Japan), Hong Kong, Macau, Singapore, South Korea and Taiwan). Southern countries refer to countries belonging to the Global South.
About Financial Transparency Coalition

The Financial Transparency Coalition (FTC) is a global civil society network working to curtail illicit financial flows through the promotion of a transparent, accountable and sustainable financial system that works for everyone. For more information, kindly visit: https://financialtransparency.org/
Opportunities and Challenges that Promote the Advocacy Efforts for the Legal Profession

A Toolkit on Illicit Financial Flows: Module 3

Advocacy Manual for Lawyers’ Association in the Global South
About the project:
As a unique space under the Financial Transparency Coalition (FTC), the Southern Regions Programme (SRP) plays a crucial role of an incubator by placing just tax systems and financial transparency at the heart of development debates. In October 2017, during a South-South strategy meeting it was recognised to bring out a collaborative document that emerged from the perspective of the Global South. Five members of the SRP came together to author the IFF Toolkit in an effort to address issues of financial secrecy, enablers of illicit financial flows, lopsided impact on domestic resources and the ability to raise further resources due to loss of revenue as IFFs and the much-needed reforms in the international financial architecture set in the context of Global South. The toolkit uses case study-based evidence to simplify the issue of tax abuse. The document also covers tax incentive abuse as a subject under IFFs. The toolkit has benefitted from discussions held at the Nepal Social Forum (March 8th-10th, 2018), Paper on Illicit Financial Flows: Rights, Restoring Justice and Freedom and Pan-Continental Southern Dialogue on Illicit Financial Flows, Nairobi (November 21-22, 2018).

Disclaimer:
The publication has been produced by the Pan African Lawyers Union (PALU) who is also a member of the Southern Regions Program in the Financial Transparency Coalition (FTC). This output does not intend to reflect the positions of all members of FTC.

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Designed by: How India Lives (www.howindialives.com)

For more information about the module, kindly write to: fgodbout@lawyersofafrica.org.
List of Acronyms

AAAA —— Addis Ababa Action Agenda
AMLA —— Anti-money laundering
FATF —— Financial Action Task Force
IBA —— International Bar Association
OECD —— Organisation for Economic Co-Operation and Development
PALU —— Pan-African Lawyers’ Union
STR —— Suspicious transaction report
TFTC —— OECD Task Force on Tax Crimes and Other Crimes
UNCTOC —— United Nations Convention Against Transnational Organized Crime
UNGA —— United Nations General Assembly

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The rule of law is a basic principle in the defence of justice, human rights and moral sanctity of the society. The legal profession has a juxtaposed role in upholding and safeguarding the rule of law. This ‘profession’ embodies three values, namely, organisation, learning and the spirit of public service. It embraces lawyers acting in accordance with higher standards. Accordingly, the ethics of the profession are public service-oriented with rewards being incidental. Lawyers are therefore key change agents with great potential to influence positive policy reforms and socio-economic development in society.

However, the nobility of the legal profession stands challenged. It is now a commercial profession driven by monetary gain and greed. Lawyers skilfully use their legal knowledge and are often seen manipulating laws to their advantage rather than pursuing justice. Commentators see lawyers as ‘enablers’ of illicit financial flows or IFFs. Enablers of IFFs can be defined as a ‘[...] heterogeneous network of professionals that flouts and uses loopholes in both national and international laws to generate and drive the cross-border outflow of illicit finance.’ Since the complexities of taxation, law and global finance make it difficult to engage with these issues, the cardinal services of lawyers are often solicited.

The International Bar Association (IBA) has noted a decline in the ethical behaviour of legal professionals. More lawyers are facilitating IFFs and abusive tax practices and are more willing to give opinions on such transactions. For example, the Panama based law firm, Mossack Fonseca, was accused of creating shell companies as proxies for its clients to evade taxes.

‘Every year huge sums of money are transferred out of developing countries illegally. These illicit financial flows strip resources from developing countries that could be used to finance much-needed public services, from security and justice to basic social services such as health and education, weakening their financial systems and economic potential. While such practices occur in all countries—and are damaging everywhere—the social and economic impact on developing countries is more severe given their smaller resource base and markets.’ IFFs are therefore a persistent challenge in the
Introduction and Background

Lawyers skilfully use their legal knowledge and are often seen manipulating laws to their advantage rather than pursuing justice. Commentators see lawyers as ‘enablers’ of illicit financial flows or IFFs. Global South. They account for substantial sums of money illegally transferred out of the Global South, stripping developing regions of resources that could have been used to finance much-needed public services such as health and education, as well as the progressive realisation of human rights. At the heart of this challenge, lies the role played by enablers or facilitators of illicit flows, including banks, accounting and auditing firms, and lawyers. There are mounting allegations against lawyers abusing their profession at the expense of the integrity of the profession by providing services in furtherance of IFFs, whether directly or indirectly. Despite this, legal expertise ranges from interpreting laws, upholding the rule of law, accounting for injustice, and holding perpetrators of economic injustice responsible for their activities in courts of law. This makes the legal profession well-placed to influence policy reform in municipal, sub-national, federal, regional and international law with regard to the fight against IFFs.

Using this Advocacy Guide

This guide highlights the important role played by lawyers in the promotion of global measures to combat IFFs by enhancing the knowledge of lawyers’ associations on the effects of IFFs in the Global South. It also provides references for lawyers’ associations on activities and strategies they can adopt to curb IFFs in the Global South and to empower lawyers as advocates who are opposed to enabling IFFs.

Basis for legal professionals’ responsibility to curb IFF’s

This aids the understanding of the matrix of regional and international legal obligations for lawyers to uphold their ethical standards and to comply with measures aimed at curbing IFFs. In return, this circumvents conflict of interest in high-risk transactions that might expose lawyers as enablers of IFFs. Since there are no specific international or regional laws on IFFs, this guide provides regional, national and international legal obligations that arise from taxes, human rights, anti-money laundering, anti-corruption, trade and investment. It also provides professional codes of conduct for lawyers, and how lawyers’ associations could help implement regional and international obligations in their jurisdictions.

Recommendations for lawyer’s associations to curb IFF’s while upholding standards of the legal profession

Lawyers’ associations must ensure that their members uphold professional standards, and protect them from intimidation and improper restrictions and infringements. Above all, lawyers’ associations have an obligation towards society to ensure that the interests of justice prevail and legal services are available to, and accessible by everyone.
The Origin of the Legal Profession’s Responsibility to Curb IFFs

Due to the nature of their duties and obligations, lawyers strategically facilitate and mediate economic and financial transactions. Thus, policies against IFFs may require lawyers to identify, understand and comply with specific statutory obligations, the nature of which is debatable based on national approaches. Thus, worth noting are the intricacies on IFFs and the secrecy underlying them.

The legal profession’s responsibility arises from two key sources, namely, domestic and international obligations aimed at upholding and promoting ethical norms for the profession. Both sources ensure that lawyers in each and every domestic jurisdiction comply with the requirements for anti-money laundering and ethical obligations. The requirements entail lawyers do not unnecessarily and unintentionally risk themselves in executing their duties. Thus, the legal profession requires its members to act diligently and avoid conflicts of interest. When acting in accordance with their mandate, lawyers have a duty to avoid dragging the profession into any criminal, unethical or illegal activities, whatsoever, in the furtherance of IFFs, whether directly or indirectly.
2.1 Legal Basis of the Legal Profession’s Responsibility to Curb IFFs

The United Nations General Assembly (UNGA) plays a fundamental role in recommending methods of curbing IFFs at the international level. It provides a framework upon which states draw guidance for implementation at the domestic level. Thus, the fountainhead of the legal profession’s mandate to curb IFFs is derived from sub-regional, regional and international instruments, both soft and hard law.

Regarding IFFs caused by illicit drug trafficking, the UNGA adopted the Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substance to address this concern. Although, the Convention did not apply or use the term “money laundering” expressly, it defined the concept of money laundering and called upon states to create provisions in domestic law to criminalise it. This marked the first international attempt to ensure states arrest and prosecute those involved in illicit drug trafficking. This mandate binds states at the international level; however, domestic institutions are to investigate, arrest and prosecute offenders before municipal courts.

Illicit drug trade creates substantial illegal income and those engaged in these activities attempt to launder such proceeds into the formal financial system. They can use front and shell corporations to hide such income or assets. Lack of transparency in the beneficial ownership of such corporations creates hurdles for anti-money laundering (AML) detection. When suspected criminals find themselves in difficult legal situations, lawyers are their saviours. Successful career criminals think ahead and need lawyers to assist with their illegal enterprise. Criminal defence therefore becomes a key service that many lawyers provide. Unethical lawyers advise such clients on how to circumvent the law by laundering ill-gotten money. A few lawyers would not resist such rewarding deals with clients and would do what no ethical lawyers would do—see business opportunities in criminal activities. Indirectly, the Convention requires the legal profession to combat IFFs.

The Convention against Transnational Organized Crime requires lawyers to act with due diligence to curb IFFs. The Convention criminalises IFFs and explicitly urges member states to consider and criminalise all acts incidental to IFFs. To ensure compliance with the directive, a mandatory requirement was made in terms of the Convention for member states to establish at domestic regulatory
When suspected criminals find themselves in difficult legal situations, lawyers are their saviours. Successful career criminals think ahead and need lawyers to assist with their illegal enterprise.

regimes and capacitate regulatory authorities as gatekeepers for IFFs. The regulatory regimes were concerned with the requirements of customer identification, record-keeping and reporting of any suspicious transactions. The Convention uses ‘a catch-all term’ where ‘other bodies susceptible to money laundering’ includes legal professionals to highlight their role as enablers of IFFs. Therefore, member states are to ensure mutual cooperation in exchange of information to curb IFFs. This also requires lawyers’ associations to participate, for instance, in drafting policy documents for implementation by their members.

In its AML provisions envisaged in the Convention against Transnational Organized Crime, the UN restated the importance of the recommendations by the Financial Action Task Force (FATF). The significance of adopting the FATF approaches is the unequivocal acknowledgement of their relevance and importance through the lens of the UN. Although the recommendations are not specifically binding on member states, their adoption by the UN provides international recognition, and potential adoption and domestication, by the member states. The adoption of FATF recommendations (discussed below) by the UNCTOC could motivate legal professionals to participate in the fight against IFFs.

**Convention against Corruption**

The Convention Against Corruption was adopted by the UNGA in October 2003 and entered into force in December 2005. This Convention is the only binding international anti-corruption multilateral instrument. It recognises the importance of both preventive and punitive measures. It deals with cross-border corruption and calls for international cooperation. States that ratified the Convention are expected to cooperate in criminal matters, including IFFs, and to investigate issues pertaining to corruption. Further, the Convention provides for the participation of civil society and non-governmental organisations in accountability processes and underlines the importance of access to information. The reason to include participation of stakeholders is most likely to counterbalance the political influences faced by the system. Thus, the Convention pushes for curbing cross-border corruption, a component of IFFs. Another objective of the Convention is to strengthen international law enforcement and judicial cooperation between member states by providing effective legal mechanisms for international asset recovery.

The illegal proceeds may be layered into the financial system in various ways (for e.g. through real estate) and these assets may further be anonymously owned through shell companies. Thus, criminals may solicit lawyers’ services to achieve their illegal goal. Accordingly, lawyers’ obligations arise to avoid formalising illegal funds. A lawyer becomes an enabler, by providing services where they suspect or have reason to believe that the fund or property in question is the product of crime.

The launch of anti-corruption strategy for legal professionals in 2010 by the International Bar Association was a milestone for lawyers was seriously affecting the nobility of the profession in the Global South.

**Convention for the Suppression of Financing of Terrorism**

The Convention for the Suppression of Financing of Terrorism (1999) is another key instrument that was adopted by UNGA in response to financing terrorism. Of much interest is that financing of terrorism has also been dealt together with money laundering. Thus, the Convention requires States to criminalise financing terrorism and freeze and seize money intended to financing terrorist activities. Further, the Convention requires States to establish additional jurisdiction over offences when committed under certain circumstances.

An analysis of the Convention brings some indirect issues to the fore of the discussion. Lawyers are potential enablers of money laundering and terrorist financing due to the nature of the service they render to clients. They are vulnerable to complex money laundering schemes due to their ability to easily switch between advising on financial matters, establishing trusts and corporate entities, conveyance and other financial transactions such as investments. In such circumstances, however, lawyers are considered authentic by...
other professionals when clients are referred to
them, confirming their supposed ‘legitimacy’ by
association.43 This presents a unique problem:
if lawyers do not carry out client due diligence
checks or report any suspicions (e.g. money
laundering or terrorist financing), they expose
unsuspecting third parties, such as financial
advisors,44 in turn creating additional problems in
the legal profession. The most affected are cross-
border international lawyers, who are subjected
to unfamiliar and uncertain money laundering
requirements.45 This is a call on lawyers to
combat, not enable IFFs, whether directly or
indirectly. However, lawyers are opposed to the
disclosure compromises attorney-client privilege
and the independence of the Bar.
Financial Action Taskforce (FATF)

Apart from the Conventions referred to above, 67 countries
established FATF in 1989. The primary objective was to set up and
promote internationally recognised standards to combat money laundering. Since 1990s, 40
FATF Recommendations have been substantially revised to incorporate new developments and to reflect the changing trends in money laundering
and terrorism.46 However, the core mandate of the FATF was changed substantially following the terrorist attacks in the USA on September 11, 2001,
to include combating the financing of terrorism.47

FATF recommendations placed a duty on legal
professionals to assist in AML and curb terrorist financing. Legal professionals are mandated in
terms of the FATF, to report suspicious dealings
when engaged in financial transactions.48 Although fundamental to curbing terrorist financing activities, the suspicious transaction report (STR) requirement flies across the
dictates of the attorney-client privilege. The duty
to report suspicious transactions violates legal
ethics, like the norms of confidentiality, trust
and professional conduct. This requirement is a
threat to the independence of the legal profession
as it makes lawyers operate like spies, state
agents or law enforcement officers. Whether the
aspect of reporting is binding on lawyers is quite
controversial and depends on each jurisdiction.
In some jurisdictions, however, to continue
representing or assisting the same client after STR
has been made results in a civil or criminal suit.49
Thus, STR can cause mistrust and inaccessibility
of lawyers due to loss of confidence by society,
adversely endangering the administration of
justice for all intents and purposes.

To understand how lawyers can be enablers of
illicit finance, it is essential to know how money
laundering can be committed. Money laundering
offences have similar physiognomies throughout
the world. There are two cardinal elements to
money laundering, namely:

- The necessary act of laundering itself, i.e.
the provision of financial services, and
- A requisite degree of knowledge or suspi-
cion (either subjective or objective) relating
to the source of the funds or the conduct of
a client.

The act of laundering is committed in circumstances
where a lawyer, notarial or other independent
legal professional engages in an arrangement
(by providing a service or product) and that
arrangement involves the proceeds of crime. These
arrangements may be business relationships of
investment management or of a fiduciary nature.50
The degree of knowledge or suspicion that is
required depends on the nature of the illicit financial
flow in question. This is present where a lawyer
knows or suspects that their

The offence is committed where a
lawyer knows or suspects that their
client is engaged in or has benefited from
an illegal activity. If lawyers or
other independent legal professionals
engage or associate with such clients
or render such services, whether
direct or indirectly, they qualify as
enablers of IFFs.

The Origin of the Legal Profession’s
Responsibility to Curb IFFs

The Global South

Advocacy Manual for Lawyers’ Association in the
Global South
How the state balances the ability to make lawyers cooperate on one hand and prioritise security and safety issues rather than individual interests of clients on the other hand, have far reaching and possibly negative consequences.

not all lawyers are actively involved in providing legal services in financial transactions, however, key vulnerabilities were identified in the FATF Recommendations. It suggests that when dealing with financial transactions that require the involvement of lawyers due to intricacies such as access to specialised legal and notarial skills and services, one may blindly assist in laundering or enabling IFFs. The operation of the lawyer-client privilege shields the suspect, obstructs investigations, and delays or prevents the arrest and prosecution of the suspect if a lawyer’s services are used.

Combating money laundering is not an easy or individualistic task but a collaborative effort of several professionals, including lawyers. This collaboration is key to solicit lawyers’ services in fighting money laundering and financing terrorism. FATF’s major concern is the requirement for legal expertise to combat money laundering. As a result, FATF 40+9 Recommendations of 2003 explicitly require lawyers to comply with the STR requirement in certain strategic areas. FATF incorporated relevant recommendations that specifically required non-financial business and professions to comply with preventive measures provided for in its Recommendations. The austerely preventive measures encouraged non-financial businesses and professions, such as the legal profession, to adhere to the fundamental requirements for customer due diligence and record-keeping.

In terms of the FATF Recommendations, the legal profession is mandated to comply with the requirement to file STR whenever there are reasonable grounds to believe that the transaction in question facilitates or legitimises movement of proceeds of illegal activities, or to finance terrorism. However, there is no mandatory disclosure of STR where a legal professional is subject to professional privilege or confidentiality. Depending on the substantive content of the municipal law of a particular jurisdiction, legal obligations arise to determine cases or matters that would ordinarily fall within the lawyer-client privilege. How the state balances the ability to make lawyers cooperate on one hand and prioritise security and safety issues rather than individual interests of clients on the other hand, have far reaching and possibly negative consequences. As a matter of principle, if not moral obligation, STR requirement is a responsibility that lawyers and other independent legal professionals can consider vis-a-vis the economic challenges and/or the negative impact of IFFs on society.

The adoption of policies and the establishment of anti-corruption institutions capture the nuances and the multi-dimensional character of the problem of corruption. It is exacerbated by secrecy, which spurs corruption. Thus, greater degrees of secrecy pose higher risks of IFFs. It erodes efforts to combat money laundering and IFFs and the effectiveness of any initiatives by lawyers.

Pan African Lawyers Union (PALU)’s Code of Ethics on Anti-Corruption and Professional Compliance Standards for Lawyers Working in Africa mandates its members to uphold the ethics of the legal profession as well as the members’ Bar Associations. The Code prescribes any conduct which compromises the integrity of the profession. Such unethical conduct includes corruption, conflict of interest, debasing of lawyer-client privilege or any conduct that spurs money laundering, whether directly or indirectly. Lawyers are encouraged to pay attention to, promote and protect the rules provided for in their domestic laws, as well as regional and international instruments in so far as the conduct of the profession is concerned. Article IX specifically bars lawyers from engaging in projects or transactions they know or ought to know originate from and/or are the destination of illicit funds. When confronted with a situation of corrupt or unethical acts, PALU encourages its members to seek guidance from the Anti-Corruption and Ethics Oversight Units established by their domestic Lawyers’ Associations or the President of the Associations.

While PALU unites African lawyers and their Bars Associations through the law, its Code of Ethics has no binding effect because it does not have mechanisms for implementation. Regardless of this weakness, it is vital in upholding the ethics of the profession and its ability to mitigate conduct that potentially further IFFs. One has to be guided by such considerations to contribute towards combating IFFs.
Advocacy Options Available to the Legal Profession

Both hard and soft international law shaped and developed the international basis for the legal profession’s responsibility to curb IFFs. It provides a framework but leaves domestication and implementation to member states. Thus, the challenges caused by IFFs in the Global South warrant urgent prioritisation.

The legal profession’s awareness regarding IFFs can be linked to achieving Sustainable Development Goals (SDGs), particularly target 16.4, which calls on states to significantly combat IFFs, and all forms of organised crime by 2030. The awareness can be generated by undertaking five key roles as lawyers’ contribution to combating IFFs.

Lawyers’ Contribution to Combat IFFs

- Strategic Litigation (3.1)
- Lobbying for IFFs Related Law Reforms (3.2)
- Commissioning and Publishing Legal Research on IFFs (3.5)
- Public Awareness of IFFs, Education and Training (3.3)
- Citizen Sensitisation Programmes (3.4)
3.1 Strategic Litigation

Strategic litigation aims to bring about broad societal changes beyond the scope of an individual case at hand. It aims to use legal means to tackle IFFs that have not been adequately addressed in law or politics. It gives a platform for society, which is economically affected by endemic corruption, money laundering and other forms of IFFs to be seen and heard, triggers discussion of, for example, the right to development that is violated by individuals though IFFs. Successful strategic litigation brings about lasting political, economic or social changes and develops existing law. This increases the progressive and precedent-setting impact of the legal action against IFFs. Strategic litigation can bring significant changes in the law, as well as public awareness by taking carefully selected IFFs cases to court. With such strategic cases, although the initial step is seeking to clarify an individual IFFs complaint before the court, however, in addition to clarifying the individual case, the aim is also to obtain justice for a whole group, which might potentially find itself in a similar situation. Thus, strategic litigation is a legal tool for bringing social, legal and political change by using high profile IFFs case. In other words, the aim is to create legal precedents.

Outcomes to Strategic Litigation

As a result of strategic litigation, the following three outcomes can be achieved:

- Develop civil society and mobilise communities
- Develop sound legal culture against IFFs
- Develop democratic values and the rule of law

3.2 Lobbying for IFFs Related Law Reforms

Lobbying for law reforms is a noble consideration and a measure to combat IFFs. Through conduction of a strategic litigation, there is a need for lobbying for law reforms and building sound approaches to:

- Bring about domestic law reforms in line with international and IFFs; policy effectiveness be aligned with international initiatives;
- Conduct risk assessments at national levels to identify the major source of IFFs;
- Establish and empower regulatory institutions through statutory enactments and provision of human and capital resources;
- Provision for protection of whistleblowers under the proposed laws;
- Transparency be mandatory in all public structures and financial dealings;
- Laws to embrace participation of all since combating IFFs involves multiple policy areas;
- Push for pragmatic policy options and recommendations for punitive remedial measures;
- Ensure that laws are interpreted, implemented, enforced and policed reasonably;
- Provision In law to compel law enforcement authorities to increase awareness proactively;
- Provision in law to compel MNCs to disclose publicly their financial statements and outlaw secrecy in public interest issues;
- Transparencies be mandatory in all public structures and financial dealings;
- Laws to embrace participation of all since combating IFFs involves multiple policy areas;
- Push for pragmatic policy options and recommendations for punitive remedial measures;
3.3 Public Awareness of IFFs, Education and Training

Public awareness against IFFs assists law enforcement agents and regulatory institutions to curb IFFs. Informing society about IFFs and their nature is vital, while reporting any suspected illicit dealings is imperative. The aim is to provide simplified information as a self-screening tool for society to distinguish between forms of illicit flows and the reasons why IFFs are considered a crime. It is important to show that pernicious interests are prejudicial to national interests, as the resources available for public services and sustainable development are undermined. Public awareness is therefore essential to demonstrate that:

- Public awareness of IFFs, education and training.
- Citizen sensitisation programmes.
- Development challenges that IFFs pose to the Global South’s economic transformation.
- Development initiatives and institutions working to build political commitment to curb IFFs should be supported.
- Resources that should circulate and be used in the country’s economy as investment and taxes should not be illegally diverted or siphoned.

Compliance with the law, and assurance that whistleblowers are protected under the law, are key determinants.

3.4 Citizen Sensitisation Programmes

- Support civil society organisations to hold political leaders to account.
- Encourage and help build national investigative capacity to tackle IFFs.
- Raising the problem of IFFs in political dialogue in order to ensure engagement that addresses the challenge; and,
- Hiring or training staff in the relevant public sector authorities to promote the technical skills needed to curb IFFs.

3.5 Commissioning and Publishing Legal Research on IFFs

- Support civil society organisations to hold political leaders to account.
- Encourage and help build national investigative capacity to tackle IFFs.
- Raising the problem of IFFs in political dialogue in order to ensure engagement that addresses the challenge; and,
- Hiring or training staff in the relevant public sector authorities to promote the technical skills needed to curb IFFs.

Develop new legal tools to support the legal profession’s lobbying, campaigns and strategic litigation. This takes various forms such as investigation reports, legal articles, op-eds and legal studies.
Opportunities and Challenges that Promote the Advocacy Efforts for the Legal Profession

Domestic lawyers’ associations are relevant and convenient platforms at the national level to discuss, adopt and implement different advocacy views. Associations in each jurisdiction are domestic platforms to discuss the challenges faced by lawyers and other legal professionals and to promote their advocacy efforts. The platforms bring together all legal professionals with the sole aim to build consensus on the role of the legal profession to curb IFFs. Two key considerations, namely, lawyer-client privilege and multinational corporations (MNCs) are important to note. The defence of privilege is often used to shield certain valuable information that would ordinarily assist investigators of IFFs.

Opportunities

and Challenges

that Promote

the Advocacy

Efforts for

the Legal

Profession

4.1 Challenges to Privilege and Confidentiality: Ethical Challenges

Two key categories of ethical misuse related to the lawyer-client privilege are vital, namely, abuses of disclosure, abuses on non-disclosure, the ethics of diligence, competence and communication, and the balancing act of legal professional duties versus wider duties.

Regarding abuses of disclosure, no lawyers or independent legal professionals voluntarily disclose facts discovered or learnt during the course of professional duty, which conceivably might damage or negatively affect the reputation of a client. However, this is frequently violated in bars and clubs. A number of lawyers indulge in storytelling or gossip regardless of their basic ethical obligations. Some legal professionals expanded their ethical violations through the use of technology like the internet to share confidential information with their peers.62 However, if lawyers indulge in unwarranted disclosures of confidential information of their clients, why would they not disclose to the relevant authorities any confidential information relating to money laundering they learnt during the course of duty? In such circumstances, the privilege or confidentiality claim can be a way to avoid disclosure of information that could be relevant to domestic security and peace or in the best interest of the public. Lawyers and independent legal professionals who espouse expansive
A number of lawyers indulge in storytelling or gossip regardless of their basic ethical obligations. Some legal professionals expanded their ethical violations through the use of technology like the internet to share confidential information with their peers.

4.2 Multinational Corporations – Challenges and Prospects

Arguably, efforts to curb IFFs are weakened by the involvement of multinational corporations (MNCs) doing business in host states. MNCs bring potential economic benefits such as employment creation, building competence and skill, stimulus for economic growth and capital injection, among others. Their size, nature and scale of operation enable MNCs to benefit substantially from economies of scale, enabling lower average costs and prices for consumers.\(^{69}\) However, it is necessary to interrogate what the Global South stands to gain from MNCs’ investments. While MNCs have become omnipresent in the Global South, there are permanent worries about their operations.

The role played by MNCs is subject to debate. MNCs are by far the biggest culprit of IFFs.\(^{66}\) They exploit loopholes in national and international laws to commit financial crimes in sophisticated ways that make them harder to detect or investigate.\(^{65}\) They employ experts and have the leverage to influence policy changes, thus promoting illicit ways of doing business in host states.\(^{68}\) When confronted with legal issues, they have top lawyers to represent them even in IFF accusations (such as tax abuse, transfer mispricing, money laundering, transfer of funds by bribery and corruption among other financial crimes).\(^{67}\) Some lawyers have MNCs as clients, and may not want their relationship to be affected as this may also affect their source of income.

The Global South in which some MNCs operate end up paying more than what was actually invested. This is done through profits, debt servicing, royalties and fees, capital flows from South to North, and manipulation of imports and export prices. Although such reverse flows are themselves not unusual, however, the element of ‘manipulation’ makes the returns unjustifiably high and therefore become illicit outflows.\(^{70}\) Lawyers are highly involved in the chain. The defence of lawyer-client privilege is not a silver bullet; it does not serve the public’s interests but that of the parties involved. Against this backdrop, lawyers are highly vulnerable as proxies and tend to benefit from the ill-considered activities of MNCs.

Outflow of Capital

The problem of IFFs is exacerbated by high levels of secrecy, weak tax administration, governance challenges, political instability and conflicts, lack of monitoring or regulatory capacity among others. Therefore, combating IFFs depends on the role lawyers and independent legal professionals play in institutionalising prudent legal regulatory regimes.

Regardless of insightful debates on the attorney-client privilege, and changes occurring in AML initiatives, the Global South continues to lose substantial resources through IFFs.\(^{64}\) The problem of IFFs is exacerbated by high levels of secrecy, weak tax administration, governance challenges, political instability and conflicts, lack of monitoring or regulatory capacity among others. Therefore, combating IFFs depends on the role lawyers and independent legal professionals play in institutionalising prudent legal regulatory regimes.

Multinational Corporations – Challenges and Prospects

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4.2.2 Tax Evaders

The principle is that all taxes should be paid to the host government of the country where economic activities in question occur and value is created. This principle was formulated and endorsed by G20 leaders in 2013, as ‘profits should be taxed where economic activities deriving the profits are performed and where the value is created’. The endorsement by the G20 leadership influenced the drafting of guidelines by OECD Task Force on Tax Crimes and Other Crimes (TFTC), which concluded in 2015. The G20 Declaration has wide-reaching international endorsement in the Addis Ababa Action Agenda (AAAA), with the statement that "we will make sure that all companies including MNCs pay taxes to the Governments of the countries where economic activity occurs and value is created, in accordance with national and international laws and policies".

In this regard, the US Chamber of Commerce in Bangkok claimed the MNCs paid 70% of Thailand’s corporate taxes. This implied considerable tax abuse by locals, clouded by the intricate workings of the local tax code. Similarly, Indonesia investigated Alphabet Inc.’s Google for alleged abusive tax practices and tax evasion from 2011 to 2015. For the 2015 tax year, Alphabet Inc. was accused of dodging $400 million in taxes.

In contrast, Singapore’s low tax and generous tax incentives regime has made it highly attractive for MNCs like Apple Inc. and Microsoft. However, due to substantial loss of revenue, Singapore’s Ministry of Finance implemented a paradigm shift in the island nation’s tax policies. The move was meant to tax MNCs’ profits derived from all activities that were performed and/or where value was created. This was a setback to MNCs’ artificial shifting of profits. The investigations prompted American business groups in the region to issue a statement. Their warning that the tax crackdown risked slowing down planned investments by MNCs was an indirect endorsement that their activities should not be interfered with. The investigation of MNCs and changes in tax policies were fundamental to closing loopholes in the tax regime and curb tax abuse.

4.2.3 Organised Crime

The introduction of well-known brands in the Global South by MNCs also ushered in irresistible ways to lure criminal organisations to branch out into this lucrative area of crime. East Asia is considered the hotbed of counterfeiting criminal activities such as smuggling, money laundering, drug trafficking and narcotics. Organised crime is a serious problem in the Global South and the emergence of international trade in counterfeit goods has provided organised crime new and highly lucrative means to earn illegal profits.

In summary, the debate regarding STR vis-à-vis legal privilege remains unsolved in many jurisdictions. Lawyers in particular strongly resist the STR requirement on the basis that it violates the legal profession (lawyer-client) privilege, which require confidentiality. Thus, the challenge caused by MNCs, as far as IFFs are concerned, is a case in point. Key professional legal skills that lawyers possess that are used in various sectors to circumvent the law and spur IFFs may also be tapped to close the gaps. The same skills and knowledge applied to enable IFFs can also be tapped in a positive way to combat IFFs.
Recommendations

Whether resulting from corruption, money laundering or tax abuse, IFFs constitute a major threat to economic development in the Global South. A majority of governments in the South are currently unable to fulfil most basic human needs. Due to its positioning in society, the legal profession, in particular lawyers, are often enablers, although at times unwittingly, of IFFs. However, if they can be enablers, lawyers can also effectively proscribe IFFs. Key measures that lawyers’ associations may adopt and implement can be a game changer—enabling the legal profession to participate in combating IFFs in the Global South.

However, due to the complex nature of IFFs, detecting and preventing corruption and money laundering pose an almost insurmountable challenge in the absence of unwavering cooperation and information sharing. Thus, the realpolitik of combating IFFs requires lawyers’ associations to court the cooperation of the entire legal profession (lawyers, notaries, conveyancers, and other independent legal professionals). Lawyers’ associations should play a cardinal role, both as policy giver to members and regulator of the profession to ensure all members—including independent, legal and professional members—in each domestic jurisdiction comply with the associations’ directives. In order to do so, it is recommended that every independent legal professional in each jurisdiction be registered with the relevant law association to ensure compliance with the association’s policies, as well as easy monitoring and regulation of their activities.

It is imperative that the legal profession combat IFFs proactively. Through cooperation, the legal profession in the Global South can strengthen anti-corruption and anti-money laundering mechanisms and curb IFFs.
Advocacy Options for Lawyers' Associations

The lawyer-client privilege serves as the cornerstone for the right to a fair trial, privacy and proper functioning of the justice system. However, the protection of the privilege must not hinder efforts to combat money laundering, corruption and financing terrorism among other IFFs. Since the legal profession occupies a cardinal role in preventing and detecting crimes, it is recommended that lawyers and other independent legal professionals should not be exempted from STR requirement. Exempting them widens the gap in AML and terrorist financing legal regime.

Further, regarding disclosing confidential information for the primary purpose of combating money laundering and financing terrorism, it is recommended that reasonable balance be struck between legal professional privilege and countering money laundering and financing terrorism. With regard to fighting money laundering, it is recommended that lawyers’ associations lobby for the adoption, uniform implementation and enforcement of the standards set by the FATF more strictly, particularly in conducting due diligence of politically exposed persons and more strictly, particularly in conducting due diligence of politically exposed persons and establishing true ownership of legal entities. Associations can lobby for transparency and accountability systems that actively and effectively address the culture of corruption and money laundering, as well as provide incentives and protection for whistleblowers.

Recommendations to the Lawyers' Associations and Legal Profession

5.1 Recommendations to the Lawyers' Associations and Legal Profession

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End Notes

24. Article 7(1) of the Palmae Convention.
27. The UN Convention Against Corruption (2003), hereafter UNCC. Promotion of Integrity, hereafter UNCC.
28. Piracy, see Chapter II, Article III of the UNCC. and Article II of the UNCC.
29. Corruption, see Article II of the UNCC.
30. Asset recovery, see Article II, Article III of the UNCC.
32. UNCC, Global Report on the Susceptibility of Financing Terrorism (2016); hereafter the GCMG Report on the Susceptibility of Financing Terrorism. The Convention was adopted by the UN General Assembly on 10 April 1999. It is currently in force for 124 States.
34. See F ATF Report Money Laundering Typologies (2000-2009)
36. Ibid.
37. Ibid.
38. Article 7(1)(a) of the Palmae Convention. Financial organisations vary widely from large, state-like organisations to small, decentralised & ill-disciplined networks. Financial organisations require control in order to discover the crimes of those branches, by stratification, by the organisation, and by creating an existing environment necessary to sustain their illegal activities.
40. F ATF Money Laundering, op cit at 16 et seq.
41. Recommendation 10 of the CSF.
42. Recommendations 22(d) & 23(a) of the F ATF.
43. The International Bar Association, et al.; see nd F ATF 13.
44. Five financial activities were referred to in Recommendation 22(d) of the F ATF Report, namely: (i) buying and selling of real estate, (ii) managing of client money, securities or other assets, (iii) organisation of contributions for the creation, operation or management of companies and/or branches, (iv) organisation or arrangement, and buying and selling of business entities.
45. Ibid.
46. Ibid.
47. F ATF Report, supra note 26 at 36.
55. Shameema Ferdausy & Md Sahidur Rahman, op cit note 66 at 199.
56. Shameema Ferdausy & Md Sahidur Rahman, op cit note 66 at 199.
58. Ibid.
61. Ibid.
62. Ibid.
64. Ibid.
71. Ibid.
72. Ibid.
73. Ibid.
75. Ibid.
77. Shameema Ferdausy & Md Sahidur Rahman, op cit note 66 at 199.
82. Ibid.
How to Use the Toolkit?

The toolkit is as an easy and accessible resource for enthusiasts, activists, civil society organisations, practitioners and journalists. Designed in a modular format, the toolkit aims to enable evidence based advocacy from the perspective of developing countries for bringing awareness, policy change, exchanging examples of effective interventions from the Global South and wider collaboration between different actors. Please note that the policy recommendations are aimed to be adapted and tailored across settings, regions and priorities.

All modules are designed independently from each other but are structured in a holistic manner. It is recommended that Module 1 be read first as it sets the premise for this undertaking. The toolkit fulfils three objectives -

- Provides a well-rounded perspective of illicit financial flows from the Global South context and delving into its regional components.
- Introduces terms that are set under the framework of human rights, gender justice and the sustainable development agenda with respect to redressing the impact of illicit financial flows.
- Uses a multi-pronged approach to involve the larger civil society, practitioners and journalists through international and regional mechanisms, simplified case studies to demystify complex topics and examples of successful interventions across the Global South.

The toolkit is available in print and online. The technical module is available in Spanish.

A Toolkit on Illicit Financial Flows: Perspectives from the South

**Module 1:** Politics of Defining IFFs

**Module 2:** IFFs and the Extractives Section in Asia

**Module 3:** Advocacy Manual for Lawyers’ Association in the Global South

**Module 4:** Addressing Illicit Financial Flows – National, Regional and Global Interventions

**Module 5:** Technical module: The Role of Banking in Latin America as a facilitator of Illicit Financial Flows

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The toolkit uses the terms developing countries or regions interchangeably with the Global South. The term "Global South" represents countries in the developing regions of Africa, Asia and Latin America, Central America, Mexico, South America, and the Middle East (with the exception of Lebanon and Turkey) that share a colonial and imperial past (with the exception of Japan, Hong Kong, Macau, Singapore, South Korea and Taiwan). Southern countries refer to countries belonging to the Global South.
About Financial Transparency Coalition

The Financial Transparency Coalition (FTC) is a global civil society network working to curtail illicit financial flows through the promotion of a transparent, accountable and sustainable financial system that works for everyone. For more information, kindly visit: https://financialtransparency.org/
Opportunities and Challenges that Promote the Advocacy Efforts for the Legal Profession

A Toolkit on Illicit Financial Flows: Module 4

Addressing Illicit Financial Flows – National, Regional and Global Interventions
About the project:
As a unique space under the Financial Transparency Coalition (FTC), the Southern Regions Programme (SRP) plays a crucial role of an incubator by placing just tax systems and financial transparency at the heart of development debates. In October 2017, during a South-South strategy meeting it was recognised to bring out a collaborative document that emerged from the perspective of the Global South. Five members of the SRP came together to author the IFF Toolkit in an effort to address issues of financial secrecy, enablers of illicit financial flows, lopsided impact on domestic resources and the ability to raise further resources due to loss of revenue as IFFs and the much-needed reforms in the international financial architecture set in the context of Global South. The toolkit uses case study-based evidence to simplify the issue of tax abuse. The document also covers tax incentive abuse as a subject under IFFs. The toolkit has benefitted from discussions held at the Nepal Social Forum (March 8th-10th, 2018), Paper on Illicit Financial Flows: Rights, Restoring Justice and Freedom and Pan-Continental Southern Dialogue on Illicit Financial Flows1, Nairobi (November 21-22, 2018).

Disclaimer:
The publication has been produced by Centre for Budget and Governance Accountability (CBGA), Latin American Network on Economic and Social Justice (LATINDADD) and Tax Justice Network Africa (TJNA) who together form a part of the Southern Regions Program in the Financial Transparency Coalition (FTC). This output does not intend to reflect the positions of all members of FTC. This work is licensed under a Creative Commons Attribution - Non-Commercial License (CC BY-NC 4.0). Any part of the toolkit on Illicit Financial Flows may be freely reproduced with appropriate acknowledgement to authors and their respective organisations. Views expressed in this publication are those of the authors.

Authors: Sakshi Rai (lead), Andres Arauz with contributions from Robert Sseuna and expert inputs from Matti Kohonen and Aida Jean Nacpil Manipon

Designed by: How India Lives (www.howindialives.com)

For more information about the module, kindly write to: sakshi@cbgaindia.org / andres.arauz@gmail.com

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1 Asian People’s Movement on Debt and Development (APMDD), Centre for Budget and Governance Accountability (CBGA), Latin American Network on Economic and Social Justice (LATINDADD), Pan African Lawyers Union (PALU) and Tax Justice Network Africa (TJNA)
## List of Acronyms

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<thead>
<tr>
<th>Acronym</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>AAAA</td>
<td>Addis Ababa Action Agenda</td>
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<td>ADR</td>
<td>Association for Democratic Reforms</td>
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<td>BPIA</td>
<td>Beijing Declaration and Platform for Action</td>
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<td>CAN</td>
<td>Andean Community</td>
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<td>CARICOM</td>
<td>Caribbean Community</td>
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<td>CAT</td>
<td>Committee against Torture</td>
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<td>CBDR</td>
<td>Common but Differentiated Responsibilities Committee</td>
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<td>CED</td>
<td>Committee on Enforced Disappearances</td>
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<td>CEDAW</td>
<td>Committee on the Elimination of Discrimination against Women</td>
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<td>CEPAL</td>
<td>Economic Commission for Latin America and the Caribbean</td>
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<td>CERD</td>
<td>Committee on the Elimination of Racial Discrimination</td>
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<td>CESCR</td>
<td>Committee on the Elimination of Racial Discrimination</td>
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<td>CGT</td>
<td>Capital Gains Tax</td>
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<td>CIAT</td>
<td>Inter-American Centre for Tax Administrators</td>
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<td>CIC</td>
<td>Central Information Commission</td>
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<td>CMW</td>
<td>Committee on Migration Workers</td>
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<td>CRC</td>
<td>Committee on the Rights of the Child</td>
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<td>CRPD</td>
<td>Committee on the Rights of Persons with Disabilities</td>
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<td>CSW</td>
<td>Committee for the Status of Women</td>
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<td>DTAA</td>
<td>Double Taxation Avoidance Agreement</td>
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<td>ECOSOC</td>
<td>Economic and Social Council</td>
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<td>FDI</td>
<td>Foreign Direct Investment</td>
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<td>FID</td>
<td>Financing for Development</td>
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<td>G8</td>
<td>General Recommendations</td>
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<td>HLPF</td>
<td>High Level Political Forum</td>
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<td>IASB</td>
<td>International Accounting Standards Board</td>
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<td>IATF</td>
<td>Inter-Agency Task Force</td>
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<td>ICESCR</td>
<td>International Covenant on Economic and Social Rights</td>
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<td>IFFs</td>
<td>Illicit Financial Flows</td>
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<td>ILO</td>
<td>International Labour Organization</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<td>IT</td>
<td>Income tax</td>
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<td>MLI</td>
<td>Multilateral instrument</td>
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<td>MNC</td>
<td>Multinational Corporation</td>
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<td>NEGB</td>
<td>Northern Economic Governance Institutions</td>
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<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<td>OHCHR</td>
<td>United Nations High Commissioner for Human Rights</td>
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<td>RTI</td>
<td>Right to Information</td>
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<td>SDGs</td>
<td>Sustainable Development Goals</td>
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<td>SICA</td>
<td>Central American Integration System</td>
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<td>SPT</td>
<td>Subcommittee on Prevention of Torture and other Cruel, Inhuman or Degrading Treatment</td>
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<td>Tax Justice Network Africa</td>
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<td>TNCs</td>
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<td>UNCAC</td>
<td>UN Convention Against Corruption</td>
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<td>UNCTAD</td>
<td>United Nations Conference on Trade and Development</td>
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<td>UNECA</td>
<td>United Nations Economic Commission for Africa</td>
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<td>UNESCO</td>
<td>United Nations Educational, Scientific and Cultural Organization</td>
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<td>UNODC</td>
<td>United Nations Office on Drugs and Crime</td>
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<td>UNSR</td>
<td>UN Special Rapporteur</td>
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<td>VNRs</td>
<td>Voluntary National Reviews</td>
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<td>World Health Organisation</td>
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- **Chapter 1** Introduction and Background
- **Chapter 2** Mapping Southern Institutions and Processed Tackling IFFs
- **Chapter 3** Engaging with Rights-Based Mechanisms
- **Chapter 4** International Human Rights Frameworks
- **Chapter 5** Regional Actions - A Peak into Latin America
- **National Actions**
- **Endnotes**
This module will examine effective interventions, mechanisms and processes employed by governments or the civil societies of developing countries to curb illicit finance on regional, national and global levels. These interventions are often prompted by scandals such as the Panama Papers or other emblematic data leaks that have revealed the extent of the illicit financial flows, and those involved in them.

However, exposing these stories alone is not enough, as it is equally important to assess alternative frameworks like human rights institutions, rapporteurs and multilateral bodies when approaching the issue. Therefore, in this module we will explore those who truly make the rules on illicit financial flows. This demands the full participation of the Global South while aligning approaches to tackle IFFs with human rights principles by focusing on those who are the most affected by it and securing their right to remedy.
he approach of international institutions, processes and mechanisms to tackle IFFs at the moment are fragmented and in different competing spaces. The five spheres of global governance show where the balance is tipped in favour of northern-based dominated bodies, while other bodies have a more even southern majority power.

For civil society in developing countries, human rights frameworks and financing the sustainable development agenda are international spaces where intersectional issues can show the impact of an unequal, unfair and a neoliberal financial system. Human rights and SDG spaces tend to have equal representation between all countries, but have a limited role in economic governance.

What is notable is that institutions that are dominated in the Global North hold most of the economic and financial power in the world, including G20, OECD, IMF and the World Bank. Whereas, developing countries hold most of the power in the UN General Assembly, where they are either a part of non-political bodies (e.g. UN Committee of Experts on International Tax Matters) or require a full consensus (e.g. UN FFD Forum).

In the human rights system we see a gradual rise in the importance of economic issues via the rapporteurs of the UN Human Rights Council. It is also important to note that the agendas of the various treaty bodies and regional human rights mechanisms are starting to increasingly provide monitoring on IFFs and related issues. In addition, the SDG specific monitoring is also starting to make an impact as IFFs is an SDG indicator. Thus, bodies like the Committee for the Status of Women (CSW) have since begun commenting on the issue.

Spaces such as regional bodies and regional institutions are where Global South has arguably the most important entry points. However, Northern countries are members of even such spaces. UN regional economic commissions, and more recently regional tax fora, are avenues for developing countries to exchange best practices on IFF matters and to develop national approaches that take into consideration their differentiated and distinct needs.

There is a challenge presented to the entire multilateral system (whether Northern, Southern or somewhat equally dominated) by private sector initiatives that rely on either multi-stakeholder approaches (like World Economic Forum), or on defining the purpose so narrowly that it excludes civil society and many governmental stakeholders entirely (IASB, which is not a public institution). They are often allowed to exist by explicit or implicit consent by Northern Economic Governance Institutions (NEGI).
One of the key ways to shift power in bodies is with equal and meaningful representation from the Global South on the issues of illicit financial flows in the context of human rights, gender equality and SDG. In this section, we will discuss different mechanisms and entry points in each process for advocating against IFFs. We will also discuss how to engage with them and the rationale behind targeting these spaces.
Commission of Status of Women

Objective
The Commission on the Status of Women (CSW) is the principal global inter-governmental body dedicated to the promotion of gender equality and the empowerment of women.

Purpose
The CSW takes the lead in monitoring and reviewing progress and emerging challenges in the implementation of the Beijing Declaration and Platform for Action (BPfA), and in gender mainstreaming in the UN.

Entry point(s)
1 As functional commission of the Economic and Social Council (ECOSOC), it is expected to be “instrumental in promoting women’s rights, documenting the reality of women’s lives throughout the world, and shaping global standards on gender equality and the empowerment of women.”

2 Evaluates progress in implementation of the 1995 Beijing Declaration for Action and the 23rd Special Session of the General Assembly held in 2000.

Advocacy cycle
Time
Meets annually for 8 weeks in March, following the commemoration of International Women’s Day (8th March).

How to Engage:
1 Engage in dialogue with governments to increase the attention on IFFs
2 Engage in regional CSW processes spearheaded by civil society groups
3 Participate as members of a country’s official delegation
4 Contribute to formulating inputs for the draft Outcome Document, in countries where this is possible
5 Organise side events on thematic issues
6 Prepare oral interventions or statements for the plenary session or Experts’ meetings
7 Participate in NGO side events

Creating Impact
→ CSW has taken an interest in the issue of illicit financial flows and its implications on gender equality and women’s empowerment agenda.

→ In 2018, in its discussion on the priority theme Empowering Rural Women and Girls, the CSW in its 62nd session noted the continuing economic marginalisation faced by rural women and overall, the multiple and intersecting forms of discrimination they encounter. The CSW emphasised the need to close resource gaps in order to address these issues:

“...The Commission reaffirms the importance of significantly increasing investments to close resource gaps for achieving gender equality and the empowerment of all women and girls, including rural women and girls, through, inter alia, the mobilization of financial resources from all sources, including domestic and international resource mobilization and allocation the full implementation of official development assistance commitments and combating illicit financial flows, so as to build on progress achieved and strengthen international cooperation, including North-South, South-South and triangular cooperation, bearing in mind that South-South cooperation is not a substitute for, but rather a complement to, North-South cooperation”

(as agreed conclusions in CSW 62, para 43).

→ In 2019 too, as CSW met for its 63rd session, it reiterated the need to plug resource gaps, including by combatting IFFs.
Our Focus - SDG Target 16.4

The SDG target 16.4 focuses on “significantly reducing illicit financial and arms flows, strengthening recovery and return of stolen assets” and cross-cuts with several other goals like:

- Poverty (goal 1)
- Gender (target 5.1, 5.2)
- Climate (goal 13)
- Inequality (target 10.1, 10.2)
- Corruption (16.5)
- Domestic resource mobilisation (target 17.1)

Indicator Process
UNODC and UNCTAD are the co-custodian agencies of target 16.4, responsible to come up with indicators, statistics and methodology. Headed by the UN STATS, the Inter Agency Expert Group on SDGs comprises of national statistical commissions and other such bodies who ultimately advice and make decisions on indicators and their progress. UNCTAD focuses on the commercial and tax related aspect of IFFs and UNODC concentrates on the criminal aspect.

- In terms of developing regions, UNCTAD has partnered with UNECA by conducting pilot studies in 9 African countries.
- In Asia-Pacific and Latin America, UNODC has taken the lead in this process.

What is the issue?
As a tier II indicator with limited parameters of identification, the target faces several conceptual, technical and methodological challenges and risks being dropped by the time of the 2020 review summit of the SDGs.

At present, there is only one indicator that has been proposed under target 16.4. It uses the proportion of legal persons and arrangements for which beneficial ownership is publicly available. The proposed indicator does not clarify if it includes all legal entities like companies, limited liability partnerships, trusts, foundations, cooperative societies and associations. While information from different public beneficial registers can prove to be useful, coming up with a single indicator is met with great challenges and in this light, a mixed list of robust indicators is preferable.
Addis Ababa Action Agenda
The SDG agenda is closely linked to the Financing for Development (FfD) process.

Timeline of the Financing for Development process

- It started with an international consultation after the Asian Financial Crisis, and the landmark ‘Zedillo Report’ that laid the foundations to the FfD agenda—foreseeing the creation of an International Tax Organisation, and taxing financial transactions among other proposals. But these did not lead to a consensus at the 1st FfD Conference in Monterrey, Mexico in 2002.

- A second FfD conference was held in 2008 in Doha, leading to the Doha Declaration that explicitly stated the need for international tax co-operation but without a tangible institutional space for this purpose.

- The 3rd FfD Summit, was held in Addis Ababa in 2015, resulting into the Addis Ababa Action Agenda (AAAA), which slightly increased the frequency of UN Tax Committee meetings, agreed to ending illicit financial flows, and also created a monitoring, follow-up and review mechanism for the FfD process in the form of the Inter-Agency Task Force (IATF) report, and the annual FfD Forum.

Addition as an Indicator for Developing Countries
National indicators on tax evasion could bridge a huge gap for developing countries in closing avenues for tax abuse as well. In 1976, an Inter-American Centre for Tax Administrators (CIAT) working group broke down major avenues for tax evasion with respect to the activities employed by transnational companies. In November 2019, UNESCAP recognised issues of tax competition and base erosion as the underlying reasons for tax evasion and IFFs. Some of these indicators identified sectors and instruments that could be used for both tax evasion and avoidance:

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Tax Evasion as an Indicator for Developing Countries
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- Shell companies and trusts used as instruments to disguise ownership, control or connection.
- Highly inventive industries which make use of the huge margin between the value of their goods, the cost of production and of volume of research and development expenditure.
- "Permanent loss makers" suggests uncommercial trading and a common control relationship with suppliers and/ or customers.

Status Quo
The Second Expert Meeting on the Statistical Measurement of Illicit Financial Flows held in 2018 identified that IFFs are a monetary measure of:

- International transfers of illicitly earned capital
- Legal capital transferred internationally for illicit purposes
- Legal capital transferred illicitly

This meeting also discussed three provisional indicators for the SDG target:

- To measure misaligned profit using country-by-country reports of multinational corporations, including both the country from where the profits are declared to where the real economic activity takes place.
- Using the aggregate data from the Common Reporting Standard framework which requires financial institutions to exchange information to confirm the citizenship of account holders with resident countries and address tax evasion by the undeclared offshore assets.
- An exposure to the risk of IFFs indicator by combining opacity of partner jurisdictions with scale measures of bilateral economic and financial relationships.

The SDG agenda is closely linked to the Financing for Development (FfD) process.

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Due to the resistance of the governments in the Global North, the 2002 FfD Conference did not agree on the formation of the ITO, but rather took a step towards agreeing that taxation constitutes a cross-border dimension. Currently, only the last point has been taken up by the OECD, who has created the Multilateral Instrument (MLI) for tax information exchange. However, it remains incomplete as most developing countries do not have access to tax information flows to be able to spot suspicious and abusive tax transactions.

Finally, Addis Ababa 3rd FfD conference also considered the creation of an international tax commission in the UN system, but it did not proceed due to the blocking by US and European states who said they would veto the entire agreement if developing countries did not withdraw their demand for tax governance. The main step forward in strengthening the FfD process was the inclusion of the annual Inter-Agency Task Force (IATF) report to monitor the entire Addis Ababa outcome, and how the FfD links to the SDGs being reviewed during the year. Then, the monitoring report was taken to the annual FfD forum where governments negotiated an annual outcome document of internationally agreed conclusions.

While it is important to push for opportunities to create a UN Tax Body through the various follow-up processes, there are many opportunities to follow-up and monitor the existing commitment concerning IFFs and linking tax co-operation and IFFs to human rights frameworks, including:

- Use potential avenues like the ILO, UNODC, WHO, UN Women to strengthen the IFF and tax cooperation as well as promoting social and economic rights with tax revenue.
- To elevate the positions of developing countries at the global follow-up. Regional follow-up should lead to formal inputs and negotiated outcomes at the regional level, which are then reflected at the global level.
- To ensure that Global South government positions and priorities are included in the annual monitoring report, and rights-based frameworks are promoted in all avenues of monitoring progress.
- To enable developing countries into setting the rules on economic governance and to raise adequate funds to resource human rights and SDG frameworks.
- Bring back focus financing SDGs—a key stumbling block—by linking the FfD follow-up process with the means of implementation under Goal 17.
Article 2.1 of the International Covenant on Economic, Social and Cultural Rights (ICESCR) says that states must devote the maximum available resources to ensure the progressive realisation of all economic, social and cultural rights as expeditiously and effectively as possible, even during times of severe resource constraints, whether caused by a process of adjustment, economic recession or other factors. The UN Convention on the Rights of Persons with Disabilities (Article 4.2) and the UN Convention on the Rights of the Child (Article 4) are both explicit about state parties’ obligations to take steps to use the maximum available resources to ensure economic, social and cultural rights. Meanwhile, the Maastricht Guidelines on violations of economic social and cultural right clarifies that a state is in violation of the Covenant if it fails to allocate the maximum of its available resources to realizing human rights. In 2014, the UN Special Rapporteur (UNSR) on Extreme Poverty and Human Rights, Magdalena Sepúlveda Carmona, devoted her final annual report to examine tax and fiscal policy as a major determinant of the enjoyment of human rights. Her report noted that while human rights obligations do not prescribe precise taxation policies, obligations under various international and regional treaties, as well as many constitutions do impose limits on the discretion of States in the formulation of fiscal policies. In order to ensure that States respect, protect and fulfill rights and in order to assist them in opening fiscal space towards the realisation of human rights, fiscal policies must be guided by the obligations taken on by states under these treaties.
International Human Rights Frameworks

Special Procedures of the Human Rights Council

**Objective**

The special procedures of the Human Rights Council are independent human rights experts with mandates to report and advise on human rights from a thematic or country-specific perspective. The system of Special Procedures is a central element of the United Nations human rights machinery and covers all human rights: civil, cultural, economic, political, and social. As of 1 August 2017, there are 44 thematic and 12 country mandates.

**Entry points**

- Special Rapporteur on the Right to Development
- Independent Expert on the effects of foreign debt and other related international financial obligations of States
- Independent Expert on the promotion of a democratic and equitable international order
- Independent expert on human rights and international solidarity
- Special Rapporteur on extreme poverty and human rights

Here, we look at some of the country monitoring and reports, by two rapporteurs in particular, who have been active in defining IFFs. In theory, almost all rapporteurs could touch upon IFFs if further submissions and engagement were made more systematically, as these feed into the development of international human rights, laws and norms around which human rights are defined.

**The Independent Experts on Foreign Debt and Human Rights**

One such appointment is the Independent Expert on the effects of foreign debt and other related international financial obligations of States. In June, 2014, Mr. Juan Pablo Bohoslavsky, a lawyer from Argentina, was appointed as the Independent Expert on Foreign Debt and Human Rights. He was given the mandate to carry out analytical research and undertake country missions, in an effort to work with Governments, the United Nations, non-governmental actors and other stakeholders on issues falling under his mandate.

Through the adoption of Resolution 25/9 the Human Rights Council also asked the Independent Expert to “continue considering the impact of illicit financial flows on the enjoyment of human rights.” The Independent Expert is tasked with carrying out country missions and engaging in dialogues with the Government, international financial institutions, UN agencies and civil society as a part of the mandate to undertake global analysis and develop practical recommendations and suggestions to the countries concerned. The Independent Expert also engages in consultations with the World Bank and the International Monetary Fund and other international development organisations.

**How to engage?**

In 2018, the Independent Expert on Foreign Debt and Human Rights delivered a strong message in his fifth annual report to the UN General Assembly, “Women carry most of the burden of austerity measures, fiscal consolidation and other economic reform policies. These measures, instead of promoting women’s human rights, add to existing structural inequality, and further entrench discrimination against women.” The evidence, analysis and recommendations presented in this report benefited from independent research and consultations with a variety of stakeholders, and other inputs including submissions from NGOs.

Submit thematic papers or studies

Creating impact
**Special Rapporteur on extreme poverty and human rights**

During successive mandates (held in the past by Magdalena Sepúlveda, and currently by Philip Alston), the special rapporteur on extreme poverty and human rights has commented on the need for states to respect their duty to collect maximum available resources for the enjoyment of human rights, as well as not impede other states in realising their revenue potential by use of harmful tax regulations, laws and practices that constrain other states from being able to collect taxes.

Sepúlveda made this point strongly in her 2013 report concerning Ireland. “Providing an avenue for high-net-worth individuals and transnational corporations to evade tax liabilities...could be contrary to obligations of international assistance and cooperation, because it can directly undermine the ability of another State to mobilise the maximum available resources for the progressive realisation of economic, social and cultural rights.” Article 21 of the Maastricht principles says that States must refrain from engaging in activity that impairs the ability of other states to comply with its own human rights commitments.

For instance, there are questions to be answered about the impact of Irish tax policy on developing countries’ ability to raise revenue in pursuit of the fulfilment of citizens’ rights. Whether Irish tax policy contravenes our obligation to respect and protect the enjoyment of human rights everywhere, which involves avoiding conduct that would foreseeably risk impairing the enjoyment of human rights by persons beyond their borders, as well as conducting assessments of the extraterritorial impact of laws, policies and practices. Beyond establishing this link between tax and human rights to demonstrate how bad tax policies, practices and MNC behaviour contribute to lower tax revenues, it is important to make recommendations and follow-up points. In Particular:

- The development of tax and fiscal policy must be grounded in the principles of human rights. Greater coherence across government departments is needed to ensure that fiscal policies comply with our human rights obligations under international law and do not promote inequitable growth, or contribute to further marginalization of people and communities or create greater inequality between men and women.

A human rights impact assessment is carried out on all aspects of the budget measures. This analysis should be published together with other budget documents (like financial costing of measures) on the Ministries of Finance website at budget time to allow for the greatest possibility of public engagement.

Fiscal policy should be subject to review for its human rights impact after an agreed-upon period.

All major changes to the tax code should always include an assessment of potential spillover impact on the Global South countries. The impact assessments should consult the affected people and trigger concrete policy actions to remedy any negative impacts discovered.

There should be mechanisms to lodge official human rights based complaints in various treaty bodies to challenge harmful fiscal policies, as well as abusive practices of Transnational Corporations (TNCs) where their behaviour deliberately abuses international tax laws and norms, and thus creates tax abuses that are considered IFFs.

**Treaty Bodies**

The human rights treaty bodies are committees of independent experts that monitor implementation of the core international human rights treaties. Each State party to a treaty has an obligation to take steps to ensure that everyone in the State can enjoy the rights set out in the treaty. Currently, there are nine human rights international treaties, and one optional protocol, from which 10 treaty bodies have been established. The treaty bodies are composed of independent experts of recognized competence in human rights, who are nominated and elected for fixed renewable terms of four years by State parties. They are:

- **Committee on the Elimination of Racial Discrimination (CERD)**
- **Committee on Economic, Social and Cultural Rights (CESCR)**
- **Human Rights Committee (CCPR)**
- **Committee on the Elimination of Discrimination against Women (CEDAW)**
- **Committee against Torture (CAT)**
- **Committee on the Rights of the Child (CRC)**

**The most relevant treaty bodies in terms of tackling illicit financial flows to this date have been the Committee on the Elimination of Discrimination against Women (CEDAW) and the Committee on Economic, Social and Cultural Rights (CESCR).**

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Given the most widely ratified UN Conventions, the Bill of Rights of Women, CEDAW today is one of the most relevant treaty bodies in terms of tackling illicit financial flows to this date. It has played many important roles in CEDAW mechanisms and processes:

- Monitoring treaty implementation, and lobbying governments for policy reforms in lieu of more effective implementation.
- Providing inputs to State parties’ reports, especially in countries where governments initiate multi-stakeholder consultations in the course of preparing reports to the Committee.
- Preparing shadow or alternative reports as direct submissions to the Committee which can serve as body of evidence to be considered by the Committee. Such shadow or alternative reports could cover all articles of the Convention or focus on one thematic issue (e.g., women’s access to social services and how they are impeded by lack of resources as a result of IFFs).
- Preparing inputs for reports by UN Country Teams or other UN entities to CEDAW in countries where these are practiced.
- South-South evaluation of Universal Periodic Review.

CEDAW was adopted by the UN General Assembly on 18 December, 1979 and entered into force on 3 September, 1981. It’s the first and only international treaty that comprehensively addresses women’s rights in all spheres—civil, political, social, economic, and cultural. Often referred to as the International Bill of Rights of Women, CEDAW today is one of the most widely ratified UN Conventions.

Given this comprehensive definition of discrimination, there is thus a case to be made for examining, through the lens of CEDAW and utilizing CEDAW mechanisms, the effects or impacts of IFFs on women and their ability to fully enjoy their human rights, the benefits of development and for the potential or actual discriminatory effects of IFFs. CEDAW’s goal is to eliminate all forms of discrimination and achieve substantive gender equality. Recognising the longstanding history of gender inequality and women’s subordination, its structural roots and the role that social and cultural norms play in perpetuating inequalities, CEDAW adopts a broad and comprehensive definition of discrimination in Article 1 as:

“any distinction, exclusion or restriction made on the basis of sex which has the effect or purpose of impairing or nullifying the recognition, enjoyment or exercise by women, irrespective of their marital status, on a basis of equality of men and women, of human rights and fundamental freedoms in the political, economic, social, cultural, civil or any other field”.

Discrimination, according to CEDAW, manifests in direct and indirect forms. Direct discrimination refers to different treatment on the basis of sex or gender. On the other hand, indirect discrimination refers to any law, policy or practice that, whether by intent or outcome, has a different effect on women and men, especially when it hinders their ability to enjoy their human rights. An economic policy or practice, for example, that affects women and men differently or that hinders women from fully enjoying their rights on a basis of equality of men and women or that reinforces or leads to further marginalization of women, would be considered discriminatory in Article 3:

“States Parties shall take in all fields, in particular in the political, social, economic and cultural fields, all appropriate measures, including legislation, to ensure the full development and advancement of women, for the purpose of guaranteeing them the exercise and enjoyment of human rights and fundamental freedoms on a basis of equality with men.”

The Committee, composed of 23 experts in various fields, meets yearly for two weeks to deliberate on reports submitted by State parties. The Committee also solicits and receives shadow or alternative reports from NGOs and other independent entities like National Human Rights Commissions that can inform their consideration of State parties’ reports. The Committee is also mandated to issue general recommendations (GRs) that elaborate on thematic or contemporary issues as well as interpret and provide advice on the Convention’s relevance and practical application. While GRs are non-binding, they represent a useful and important body of norms.

NGOs and civil society organizations historically have played many important roles in CEDAW mechanisms and processes:
Unlike the high level commitments and strong regional institutions in Africa, the Latin American and Caribbean region is facing a setback in terms of regional integration. Ministers meet more frequently in Inter-American institutions in Washington rather than within the Region. Recent initiatives such as the Bank of the South, the Union of South American Nations and the Community of Latin American and Caribbean States have been, quite literally, sacrificed, in favour of Washington-based institutions and sub-regional fora such as the Andean Community (CAN), Central American Integration System (SICA) or the Caribbean Community (CARICOM). Therefore, civil society organisations have had to lead and create new fora to interact with regional policymakers. Additionally, governments and the civil society have had to fall back on regional anchors of the UN such as the Economic Commission for Latin America and the Caribbean (CEPAL).

Regional or sub-regional groups can be of formal or informal nature. They are credible spaces for civil society groups to come up with possible solutions and recommendations on the impact of IFFs and the base erosion practices of MNCs.
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Regional Actions - A peak into Latin America

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Parliamentarians

Strategy
Establishing a network of Latin American and Caribbean parliamentarians that become champions on issues of IFFs is an important step for civil society organisations.

Initiatives
Latinadd and Fundación SES organise the regional Seminar of Parliamentarian for tax justice. It is an opportunity to prioritise and educate them on issues of IFFs.

Adapting it in your context
In the absence of regional platforms, civil society organisations can take such initiatives nationally and build similar platforms.

CIAT

Strategy
The Inter-American Centre for Tax Administrations (CIAT) continues to be a good forum for tax policy coordination and horizontal cooperation between tax administrations. CIAT is a highly technical organisation that promotes knowledge exchange among its members. CIAT continues to be a strong ally in regional spaces to combat IFFs.

Initiatives
Civil society organisations in the region have advocated for strengthened exchange of experiences between tax administrations in Latin America and the Caribbean.

Adapting it in your context
Civil society can pursue sub-regional anti-money laundering groups or existing tax cooperation fora to facilitate communication between tax administrations of developing countries.

CEPAL

Strategy
CEPAL has a permanent staff and a research agenda dedicated to studying IFFs.

Initiatives
SDG regional forums are good target spaces to provide inputs. The LAC Forum on Sustainable Development organised by CEPAL likewise is a welcome space.

Adapting it in your context
Civil society groups can actively participate on issues of IFFs and human rights to further the voices from the Global South. These are also helpful spaces to engage with the regions’ trade unions, grassroots organisations and social movements.

Actors in Latin America to engage with
Before delving into creating spaces for advocacy and actions, we first set the issue of IFFs in a local context. We also look into cases where such interventions have proven to be useful. These include transparency and anti-corruption led initiatives, human rights legislations, judicial activism, tax and budget advocacy, grassroots campaigns and collaboration with journalists.

Right to Information and other Human Rights legislation

Also known as Freedom of Information, the Right to Information is fundamental to a participative democracy and enables efficient delivery of public services. Even in the absence of a request, the South African law for example, mandates public authorities to proactively publish information...
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Regions with Access to Information Laws

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<th>Region</th>
<th>Countries with Access to Information Laws</th>
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<tr>
<td>African Union</td>
<td>21 out of 45</td>
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<tr>
<td>South Asia</td>
<td>7 out of 8</td>
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<tr>
<td>Central Asia</td>
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<td>Pacific (includes Australia and New Zealand)</td>
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Public Interest Litigation of

Public Interest Litigation of

on public services. Not only used for promoting good practices, it is also used to pressurise enforcement agencies. RTI laws are therefore at the centre of fulfilling SDG target 16.6 which aims to “develop effective, accountable and transparent institutions at all levels”. Journalists, public prosecutors and transparency activists are at the forefront of exposing illicit practices, often risking their own lives.

Bringing Transparency in Political Financing

India’s Right to Information Act (2005) allows disclosure of information if public interest can be established. Transparency in political financing is crucial for a functioning and active democracy. Political financing is especially prone to attracting funds from illicit means. In India, political parties are financed through electoral trusts that are not-for-profit entities essentially meant to ensure transparency and accountability in political parties. In 2014, An RTI application made to the Income Tax (IT) department on behalf of the Association for Democratic Reforms (ADR), a non-governmental organisation, sought disclosure of the names and addresses of all the Electoral Trusts and other charitable trusts formed from Assessment Year 2003-04 and 2013-14. The application also sought audit reports, the details of contributions received by electoral trusts and distributed to political parties and the terms of income tax exemptions as claimed by these trusts. The IT department however, refused to provide the information sought on the grounds that this information was held in a fiduciary capacity and argued that there was no interest in public disclosure of this personal information. Challenging this decision, the appellant argued that electoral trusts have a legal duty to furnish this information in the spirit of transparency of political financing which is a matter of public concern. Moreover, the privacy grounds cited by the IT department applied to natural persons and not legal persons. The argument made by ADR requested that political parties be treated as public authorities and should therefore come under the RTI Act.

Upon reviewing, the Central Information Commission (CIC) in 2013 held that electoral trusts and their further distribution to political parties is not personal information. It was further held by Income Tax Department in fiduciary capacity. Financial contributions made to any political party, auditing reports and their income tax returns must be disclosed in a timely manner. Despite the CIC order, major political parties have failed to comply with this order.

Public interest litigation is a highly effective tool for civil society or private individuals to realise public justice. Public interest litigation means a legal action initiated in a court of law for the enforcement of public interest or general interest in which the public or class of the community have pecuniary interest or some interest by which their legal rights or liabilities are affected.

Article 88 of the Constitution of Nepal 1990 and article 107 of the Interim Constitution of Nepal, 2063 (year 2006 in Gregorian calendar) have provisions designed to help the development of PIL in Nepal. Forum for Protection of Public Interest (Pro-Public) is one of the first organisations in Nepal which has been working for public interest with high rate of successful Public Interest Litigations.

In April 2019, a group of Nepali individuals filed a public interest litigation against NCell Private Limited (Case 074-WO-0475), to essentially recover the full tax charge with late interest and fines, that then would amount to NPR63 million. The treaty included clauses on issues such as business profits, dividends, interest, capital gains tax and others that are inconsistent with the UN Model Double Taxation DTAA negotiations between developing and developed countries. The clauses and the stipulations within them directly weaken Kenya’s ability to achieve the much-needed revenue targets.

Thirdly, Kenya’s ability to tax the profits of foreign enterprises is further limited if the foreign firms set up a subsidiary within Kenya that trades with a parent company in Mauritius as its host country or country of origin. This legally allows foreign companies to avoid sales taxes contrary to the UN Model Convention rules.

The exclusion of potential sources of revenue and creation of loopholes from taxes such as Capital Gains Tax (CGT) through swapping of assets with no real value created would allow deceitful reporting on sales activities.

This violates accounting principles and encourages a lot of more speculative ventures over productive activity that Kenya desperately needs for its structural transformation in attaining the SDGs.

Court Ruling
Notwithstanding these technical arguments, TJNA further questioned the constitutionality of the DTAA with respect to public participation. The TJNA has also targeted Kenya and Mauritius’ adherence to the Treaty Making and Ratification Act of 2012 by lodging a case in the High Court of Kenya against the Government of Kenya (GoK) in 2014.

The Kenyan government’s failure to subject the DTAA to the Treaty Making and Ratification Act (2012) was in breach of Articles 10 (a, c, and d) and 201 of the Kenyan Constitution. It asked the Court to order the Cabinet Secretary to withdraw the legal notice 59 of 2014 and commence the ratification process afresh in line with provisions of the Treaty Making and Ratification Act (2012).

The case sought to demonstrate that the Government of Kenya’s (GoK) decision to sign the agreement carried both technical risks as well as constitutional shortcomings for Kenya. The principal aim of this suit was to show the court that there are inherent risks undermining Kenya’s ability to tax both individuals and multinational corporations (MNCs) because of the DTAA, therefore harming current tax revenue collection efforts.

In March 2019, the High Court ruled that the DTAA that Kenya signed with Mauritius was void in its breach of Section 11 (4) of the Statutory
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A Toolkit on Illicit interest litigation and advocacy. This should be the challenges posed by DTAs in their public pointing out both technical and legal aspects of Going forward, civil society first needs to continue supports any technical arguments made. Lessons Learnt

The High Court ruling was a significant outcome for the examination of the DTAA issue in Africa. It set a precedent for further scrutiny of DTAs on a technical and constitutional basis for consideration across the continent and other developing countries. It offers hope for public litigation as a policy advocacy strategy in speaking out against the different methods of capital flight from Africa in current times. The High Court ruling was also a call on civil society actors to gather evidence that supports any technical arguments made.

Going forward, civil society first needs to continue pointing out both technical and legal aspects of the challenges posed by DTAs in their public interest litigation and advocacy. This should be explicit and clear when submitting to court and in the mobilisation of public awareness.

Asset Recovery Initiatives

Asset recovery is a process defined under the UN Convention Against Corruption (UNCAC) in reference to recovering the proceeds of corruption. It has many processes including tracing, freezing, confiscation, and repatriation of proceeds stolen in foreign jurisdictions—making it a complicated and lengthy process. Coordination and cooperation between multiple agencies is a fundamental aspect of any asset recovery initiative. One of the most notorious cases was that of Sani Abacha, former president of Nigeria that involved a recovery of $1.2 billion, a process that involved assistance from multiple jurisdictions including Switzerland, Jersey, and Liechtenstein. To recover Nigerian assets, the Swiss government designated the Abacha family a “criminal organisation”, allowing it to bypass its judgement to the constitutionality of the Instruments Act 2013. But the High Court limited the mobilisation of public awareness. Legal Assistance request. Third, legal processes must usually be initiated in the requested country in order to confiscate the assets. Following this, the requested authorities must repatriate the assets back to the requesting country.

Many in civil society estimate asset recovery initiatives to be extremely ineffective due to the constraints put on the process. The lack of public beneficial ownership data or public company reporting data to better understand who may be benefiting from economic activity—and whether corruption was involved also adds to the problem. In very few cases, such as the proceeds of the late Philippine president Marcos, lead to a process of reparations where victims are paid out damages from the stolen assets recovered from foreign jurisdictions.

Tax and Budget advocacy to tackle IFFs

Fiscal policies have various avenues that can lead to IFFs either by accident or by design. Parliaments are sometimes manufacturers of tax loopholes, incentives ripe for abuse or other matters to appease special interest groups and foreign investors alike. It is not known what special deals, if any, some companies have been given, although the government has committed to publishing details of agreements signed with companies in the mining sector. Various estimates have been made on revenue losses from tax incentives in recent years. Estimates in Tanzania suggest that incentives given to corporations (only) may amount to at least $300 million, and perhaps much more. Dedicating precious resources during a short time window for the intensive budgeting phase is a crucial element. Making tax expenditure visible in binding national expenditure budgets is absolutely crucial in the narrative of tax justice and transparency, as well as improving revenue forecasting to make tax revenue more predictable. Including IFF estimations as annexes in national budget reports can be powerful metrics, much like the tax incentive estimates presented in budgets. Likewise, on the revenue side, demonstrating the biases and shortfalls of tax policy are equally important and thus estimates of the “tax gap” are also important to account for the estimated uncollected revenue from various taxes and measures to combat such tax gaps.

Budget monitoring can also be sector specific such as focusing on health, education or area specific such as social protection budgets, or budget allocations for agriculture or water and sanitation. Some budget monitoring groups

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Instruments Act 2013. But the High Court limited its judgement to the constitutionality of the arguments presented by TUNA. It, however, neither dismissed nor disagreed with technical arguments about the potential revenue losses that may accrue from the DTAA. The High Court stated that it was important to show how much the country stands to lose after signing the agreement, with examples of companies that are evading taxes. It offers hope for public litigation as a policy advocacy strategy in speaking out against the different methods of capital flight from Africa in current times. The High Court ruling was also a call on civil society actors to gather evidence that supports any technical arguments made. It offers hope for public litigation as a policy advocacy strategy in speaking out against the different methods of capital flight from Africa in current times. The High Court ruling was also a call on civil society actors to gather evidence that supports any technical arguments made. 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National Actions

Curb IFFs and ensuring that actions on IFFs lead to positive outcomes for the realization of all human rights require the political will by governments and multilateral institutions, the presence of strong legal and normative frameworks, and effective and transparent governance mechanisms. Vital to all of these is a vigilant citizenry who call on governments and international bodies to be accountable, monitor the implementation of commitments, represent peoples’ interests in decision-making processes, and exert public pressure to effect needed changes in policies or structures.

Journalist Collaboration

Providing training for journalists in IFF is a key component in the strategic collaboration between civil society groups and journalists. Investigative techniques, data mining and source-protection are all important components of this training. Additionally, civil society can aid journalists in making sense of large leaks of information. On the other hand, journalists can use reports derived from leaks to extend the relevance of the news for a period of time. Finally, civil society can take advantage of the juncture created by the reporting to educate society on IFFs and promote the transparency-focused solutions.

Global Impacts of illicit Financial Flows on Women’s Rights and Gender Justice

Gender impacts of IFFs tend to be understood and studied at the national and even local level, rarely in their global impact as an obstacle to the realization of women’s rights and gender justice.

Impact on delivery of social service

Failure to mobilize public resources affects public service delivery, increasing women’s unpaid care burden.

Unemployment and under investment in the economy

Lack of public investment leads to lack of employment creation and greater unemployment, hitting women particularly hard.

Regressive fiscal policies

IFFs often trigger regressive tax policies that have a negative effect on informal workers and people living in poverty—the majority of whom are women—as they spend a large part of their income on taxes for the essential goods and services they consume.

Reliance on debt and development cooperation

Hidden wealth increases over-dependence on overseas development assistance between developed and developing countries under strict conditionalities, hindering self-determined development priorities including those to mitigate gender inequality.

Threat to women’s peace and security

IFFs thrive on conflict and criminal activity providing financial resources behind conflict and militarization that affect women disproportionately.

Resourcing for women’s rights and gender justice

Hidden resources of illicit financial flows contravene the obligation of States to mobilize the maximum available resources for the realization of human rights, including women’s rights.
Several collaborative efforts are already underway in Latin American countries. The most successful examples are leaks ps and mexicoleaks.mx, where a group of alternative media outlets establish a secure platform for whistleblowers. Many reports are directly related to IFFs. At a regional scale, the promoters will most likely collaboratively scale the initiative to a regional platform. Public policy initiatives derived from this collaboration will most likely lead to incentives schemes where IFFs can be made from these efforts. The Value of Alternative Processes

Existing mechanisms rely on the state on curbing illicit financial flows that are perpetuated by large-scale actors such as transnational corporations and wealthy elites who arguably also have substantial political power and influence to also lobby to maintain illicit financial flows as they are in place. The political economy of illicit financial flows is such that it requires looking beyond state governance to create non-state governance and accountability processes which are aimed at larger public interest.

The 1995 BPPA is the key global policy document on gender equality which was adopted in 1995 at the Fourth World Conference on Women. Agreed Conclusions and recommendations of the CSW are forwarded to the ECOSOC for follow-up. See here: http://www.unwomen.org/en.

As of October 2019
5. UNESCAP (2019): Strengthening Regional Tax Cooperation in Asia and the Pacific, Second Session Committee on Macroeconomic Policy, Poverty Reduction and Financing for Development
10. The 1995 BPPA is the key global policy document on gender equality which was adopted in 1995 at the Fourth World Conference on Women. Agreed Conclusions and recommendations of the CSW are forwarded to the ECOSOC for follow-up. See here: http://www.unwomen.org/en.
How to Use the Toolkit?

The toolkit is an easy and accessible resource for enthusiasts, activists, civil society organisations, practitioners and journalists. Designed in a modular format, the toolkit aims to enable evidence-based advocacy from the perspective of developing countries for bringing awareness, policy change, exchanging examples of effective interventions from the Global South and wider collaboration between different actors. Please note that the policy recommendations are aimed to be adapted and tailored across settings, regions and priorities.

All modules are designed independently from each other but are structured in a holistic manner. It is recommended that Module 1 be read first as it sets the premise for this undertaking. The toolkit fulfills three objectives -

- Provides a well-rounded perspective of illicit financial flows from the Global South context and delving into its regional components.

- Introduces terms that are set under the framework of human rights, gender justice and the sustainable development agenda with respect to redressing the impact of illicit financial flows.

- Uses a multi-pronged approach to involve the larger civil society, practitioners and journalists through international and regional mechanisms, simplified case studies to demystify complex topics and examples of successful interventions across the Global South.

The toolkit is available in print and online. The technical module is available in Spanish.

A Toolkit on Illicit Financial Flows: Perspectives from the South

Module 1: Politics of Defining IFFs

Module 2: IFFs and the Extractives Section in Asia

Module 3: Advocacy Manual for Lawyers’ Association in the Global South

Module 4: Addressing Illicit Financial Flows – National, Regional and Global Interventions

Module 5: Technical Module: The Role of Banking in Latin America as a Facilitator of Illicit Financial Flows

End Notes


About Financial Transparency Coalition

The Financial Transparency Coalition (FTC) is a global civil society network working to curtail illicit financial flows through the promotion of a transparent, accountable and sustainable financial system that works for everyone. For more information, kindly visit: https://financialtransparency.org/
Technical Module: The Role of Banking in Latin America as a Facilitator of Illicit Financial Flows
A Toolkit on Illicit Financial Flows: Module 5

The Role of Banking in Latin America as a Facilitator of Illicit Financial Flows

About the project:
As a unique space under the Financial Transparency Coalition (FTC), the Southern Regions Programme (SRP) plays a crucial role of an incubator by placing just tax systems and financial transparency at the heart of development debates. In October 2017, during a South-South strategy meeting it was recognised to bring out a collaborative document that emerged from the perspective of the Global South. Five members of the SRP came together to author the IFF Toolkit in an effort to address issues of financial secrecy, enablers of illicit financial flows, lopsided impact on domestic resources and the ability to raise further resources due to loss of revenue as IFFs and the much-needed reforms in the international financial architecture set in the context of Global South. The toolkit uses case study-based evidence to simplify the issue of tax abuse. The document also covers tax incentive abuses as a subject under IFFs. The toolkit has benefitted from discussions held at the Nepal Social Forum (March 8th-10th, 2018), Paper on Illicit Financial Flows: Rights, Restoring Justice and Freedom and Pan-Continental Southern Dialogue on Illicit Financial Flows1, Nairobi (November 21-22, 2018).

Disclaimer:
The publication has been produced by Latin American Network on Economic and Social Justice (LATINDADD), which is part of the Southern Regions Program in the Financial Transparency Coalition (FTC). This output does not intend to reflect the positions of all members of FTC.

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Views expressed in this publication are those of the authors.

Authors: Andres Arauz

Designed by: How India Lives (www.howindialives.com)

For more information about the module, kindly write to: andres.arauz@gmail.com

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1 Asian People’s Movement on Debt and Development (APMDD), Centre for Budget and Governance Accountability (CBGA), Latin American Network on Economic and Social Justice (LATINDADD), Pan African Lawyers Union (PALU) and Tax Justice Network Africa (TJNA)
List of Acronyms

ASB — Atlantic Security Bank
BCP — Banco de Crédito del Perú
BIS — Bank for International Settlements
BIT — Bilateral Investment Protection
CIMA — Cayman Islands Monetary Authority
CNBV — Mexican National Banking and Securities Commission
FBI — Federal Bureau of Investigation
FIBA — Florida International Bankers Association
FinCEN — Financial Crimes Enforcement Network
FTA — Free Trade Agreements
GATS — Financial Services Annex of the General Agreement on Trade in Services
ICBC — Industrial and Commercial Bank of China
IMF — International Monetary Fund
NAFTA — North American Free Trade Agreement
SEC — Securities and Exchange Commission

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Illicit financial flows, when not in cash, are accounting movements in the (electronic) books of one or more banks. As explained in Module 1, the term “illicit” includes any transaction that is illegal or abusive in terms of its nature, origin, transfer, use or destination. However, accounting movements that require banks to go through jurisdictions based on convenience and not “economic reality” also fall within the scope of illicit activities. This implies that illicit financial flows inevitably have a cross-border feature important for tax, regulatory, secrecy, or jurisdictional arbitrage. In some of these jurisdictions, financial regulations are so lenient that (shell) banks can operate there without requiring a physical presence. When an international transfer occurs, it is generally registered in the SWIFT messaging system: a secure communications protocol used amongst thousands of banks to communicate and authorise credits or debits of accounts. The cross-border characteristic of illicit financial flows, therefore, subjects them to the conventions of the international banking correspondence system, including their denomination being an international currency—primarily the US dollar—and the use of the SWIFT messaging system. To sum up, illicit financial flows are recorded through (shell) banks in jurisdictions for convenience, in dollars and are communicated through SWIFT.

There is no publicly available analysis of SWIFT messages for Latin American and Caribbean countries, but it is possible to understand the rationale by looking at the case of Africa2.
Although, only 10% of the payments originating in Africa are channeled to North America as the final destination, North American banks are intermediaries of 40% of all international payments ordered by African banks. That is, for every ten transactions originating from Africa to anywhere in the world, four transactions go through banks in North America but only one ends up in North America. On the other hand, out of all the transactions intermediated by US banks that have originated in Africa, 35% of transactions end up in Asia-Pacific and 20% end up back in Africa. This clearly shows the central role that US banking system plays in cross-border flows, including for illicit flows.

In Latin America and the Caribbean, the relative use of the US dollar and US banks is much more frequent than in Africa, where there is still a significant influence of European banks. This is evident by the fact that the most recurring location for the General Assemblies of the Latin American Federation of Banks is Miami, USA.

Accounting movements that require banks to go through jurisdictions based on “convenience” and not “economic reality” also fall within the scope of illicit activities.

In the case of Latin America, most illicit financial flows are concentrated in the United States, Panama, the Cayman Islands and some other jurisdictions. However, if we analyse each country, there are some favourite corridors of illicit financial flows depending on geographical proximity and historical idiosyncrasies of each country’s elites. For example, Colombia and Ecuador have a close financial relationship with Panama. Argentina’s financial relationship is closer with Uruguay. Mexico has a closer financial relationship with the United States and Brazil has one with the Cayman Islands. In the next section, we examine these relationships with the help of some statistics.
General Analysis of the Situation in Latin America and the Caribbean

According to the Bank for International Settlements (BIS), Switzerland, the total deposits made by developing Latin American and Caribbean countries in foreign banks add up to a total of $403.5 billion (as of December 2018). This is in stark contrast with the $620.4 billion that Latin American and Caribbean countries have in debts with these institutions.

Before continuing with more data, it is worth highlighting a statistical problem of significant magnitude. The BIS statistics compiled by the monetary authorities of the main financial centers are limited to considering residence as “immediate counterparts”. So, let’s say, a Chilean individual creates, and is the ultimate beneficiary of a company in the British Virgin Islands, a well-known tax haven. Any monetary deposits made by this company in the United States will be recorded in statistical data as a deposit corresponding to the British Virgin Islands, not Chile. Therefore, the figures indicated in the preceding paragraph are important underestimations, but (for now) impossible to determine exactly.

The graph below shows the historical evolution of Latin America and the Caribbean’s deposits abroad. While in 1977, it did not exceed $50 billion, in 2013 it reached its highest point with $500 billion. The red line represents the deposits of the non-financial sector, that is, of companies, households and parastatal entities. That amount, as shown, reaches $146.0 billion (36% of the total). The difference between $403.5 billion and $146 billion is attributed to the financial sector’s assets that are abroad.

Figure 2: Deposits abroad of total (red) and non-financial (blue)

Source: Locational Banking Statistics - Bank for International Settlements (BIS)
The country that has the most assets abroad is Mexico, followed by Brazil, Panama and Venezuela. The case of Panama (*) is special because it is not considered to be a developing Latin American country by the BIS, but rather an offshore center. However, it is important to show the size of Panama’s nominal assets abroad in relation to the rest of Latin American countries.

If we want to observe the assets abroad of the non-financial sectors of the Latin American countries, similar results can be observed in ordinal terms. Again, we see Mexico leading, but Panama ranks even higher here than in the previous table. This is likely explained by the statistical phenomenon described above as Panama is a tax haven in which many shell companies are registered.

### Figure 3: Foreign Deposits of Residents of Latin American Countries

<table>
<thead>
<tr>
<th>Country</th>
<th>Foreign deposits (USD Billion, Dec 2018)</th>
<th>Share in Latin America (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mexico</td>
<td>117.7</td>
<td>29.20%</td>
</tr>
<tr>
<td>Brazil</td>
<td>74.7</td>
<td>19.50%</td>
</tr>
<tr>
<td>Panama*</td>
<td>54.0</td>
<td>13.40%</td>
</tr>
<tr>
<td>Venezuela</td>
<td>28.7</td>
<td>7.10%</td>
</tr>
<tr>
<td>Chile</td>
<td>27.4</td>
<td>6.80%</td>
</tr>
<tr>
<td>Peru</td>
<td>26.7</td>
<td>6.60%</td>
</tr>
<tr>
<td>Argentina</td>
<td>21.6</td>
<td>5.30%</td>
</tr>
<tr>
<td>Colombia</td>
<td>18.2</td>
<td>4.50%</td>
</tr>
<tr>
<td>Uruguay</td>
<td>12.7</td>
<td>3.10%</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>7.3</td>
<td>1.80%</td>
</tr>
<tr>
<td>Ecuador</td>
<td>6.5</td>
<td>1.60%</td>
</tr>
<tr>
<td>Bolivia</td>
<td>6.2</td>
<td>1.50%</td>
</tr>
</tbody>
</table>

Source: Locational Banking Statistics - Bank for International Settlements (BIS)

### Figure 4: Foreign Deposits of non-financial sectors of residents of Latin American Countries

<table>
<thead>
<tr>
<th>Country</th>
<th>Foreign deposits (USD Billion, Dec 2018)</th>
<th>Share in Latin America (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mexico</td>
<td>41.6</td>
<td>28.50%</td>
</tr>
<tr>
<td>Panama*</td>
<td>27.2</td>
<td>18.60%</td>
</tr>
<tr>
<td>Brazil</td>
<td>19.3</td>
<td>13.20%</td>
</tr>
<tr>
<td>Venezuela</td>
<td>17.1</td>
<td>11.70%</td>
</tr>
<tr>
<td>Argentina</td>
<td>14.9</td>
<td>10.20%</td>
</tr>
<tr>
<td>Peru</td>
<td>8.1</td>
<td>5.50%</td>
</tr>
<tr>
<td>Chile</td>
<td>7.8</td>
<td>5.40%</td>
</tr>
<tr>
<td>Colombia</td>
<td>6.3</td>
<td>4.30%</td>
</tr>
<tr>
<td>Uruguay</td>
<td>4.0</td>
<td>2.70%</td>
</tr>
<tr>
<td>Ecuador</td>
<td>3.0</td>
<td>2.10%</td>
</tr>
<tr>
<td>Guatemala</td>
<td>2.4</td>
<td>1.60%</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>2.3</td>
<td>1.60%</td>
</tr>
</tbody>
</table>

Source: Locational Banking Statistics - Banco de Pagos Internacionales (BIS)
What is the Preferred Banking System for Foreign Capital Deposits of Developing LAC Countries?

According to the Treasury Information Capital System of the US government, approximately $241.6 billion of the $403.5 billion are deposited in the United States (60% of all LAC money abroad is in the US). In the case of non-financial capital, there are $124.1 billion in the US (85%).

The amount of assets abroad, along with the information available on international payments in the case of Africa, should call our attention to the role that the United States plays in the channelling of illicit financial flows in the case of Latin America too. The largest banks in Latin America and the Caribbean are part of the Florida International Bankers Association (FIBA). The following table shows the list of FIBA member banks. Latin American owned banks and megabanks are highlighted below.

**Figure 5: Banks members of the Florida International Bankers Associations**

<table>
<thead>
<tr>
<th>Bank Name</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apollo Bank</td>
<td></td>
</tr>
<tr>
<td>Bac Florida Bank</td>
<td>Centroamérica</td>
</tr>
<tr>
<td>Banco Azteca S.A. Institución de Banca Múltiple</td>
<td>México</td>
</tr>
<tr>
<td>Banco de Bogotá Miami Agency</td>
<td>Colombia</td>
</tr>
<tr>
<td>Banco de Crédito del Perú-Miami Agency</td>
<td>Perú</td>
</tr>
<tr>
<td>Banco de Crédito e Inversiones</td>
<td>Chile</td>
</tr>
<tr>
<td>Banco do Brasil</td>
<td>Brasil</td>
</tr>
<tr>
<td>Banco Financiera Comercial Hondureña (Int’l Rep Office</td>
<td>Honduras</td>
</tr>
<tr>
<td>Banco Internacional de Costa Rica, S.A.</td>
<td>Costa Rica</td>
</tr>
<tr>
<td>Banco Pichincha</td>
<td>Ecuador</td>
</tr>
<tr>
<td>Banco de la Nación Argentina</td>
<td>Argentina</td>
</tr>
</tbody>
</table>

Latin America owned banks

Megabanks
What is the Preferred Banking System for Foreign Capital Deposits of Developing LAC Countries?

Banco Sabadell, Miami Branch  
Banesco  
Bank Hap-salim, B.M.  
Bank Leumi  
Bank of America Merrill Lynch  
Bank United Inc  
Bansirul Miami Branch  
Barclays  
BBVA Compass Group  
Brickell Bank  
Brown Brothers Harriman & Co  
Citibank, N.A-Wealth Management  
City National  
CorpBanca  
Credit Agricole Private Banking Miami  
Davivienda International  
Eastern National Bank  
EFG Capital International Corp.  
First Citizens Bank Limited  
Gibraltar Private Bank & Trust  
Global Bank of Commerce Limited  
HSBC Private Bank International  
IDBBANK-Israel Discount Bank of New York  
International Finance Bank  
Itau Private Bank  
JP Morgan Chase  
Mercantil Comercibank, N.A.  
Morgan Stanley  
Nodus International Bank  
Banco Sabadell, Miami Branch  
Banesco  
Bank Hap-salim, B.M.  
Bank Leumi  
Bank of America Merrill Lynch  
Bank United Inc  
Bansirul Miami Branch  
Barclays  
BBVA Compass Group  
Brickell Bank  
Brown Brothers Harriman & Co  
Citibank, N.A-Wealth Management  
City National  
CorpBanca  
Credit Agricole Private Banking Miami  
Davivienda International  
Eastern National Bank  
EFG Capital International Corp.  
First Citizens Bank Limited  
Gibraltar Private Bank & Trust  
Global Bank of Commerce Limited  
HSBC Private Bank International  
IDBBANK-Israel Discount Bank of New York  
International Finance Bank  
Itau Private Bank  
JP Morgan Chase  
Mercantil Comercibank, N.A.  
Morgan Stanley  
Nodus International Bank  

Northern Trust Company  
Ocean Bank  
Pacific National Bank  
Regions Bank  
Sahra National Bank of New York  
Santander Bank  
St. Kitts Nevis Anguilla National Bank Ltd.  
Sunstate Bank  
SunTrust Banks, Inc. Miami  
TD Bank  
Terrabank, N.A.  
Totalbank  
U.S Century Bank  
UBS AG  
Wells Fargo Bank, N.A.

Against this backdrop, it is not surprising that the financial intelligence unit of the US (Financial Crimes Enforcement Network, FinCEN) issued a geographically targeted order in 2016 aimed at controlling money laundering, specifically in Miami. More recently, in March 2019, the Federal Bureau of Investigation (FBI) announced the opening of an office in Miami specifically dedicated to studying accounting corruption and white-collar crimes that are conducted outside the United States but have a connection with Miami, presumably as a financial center. Miami’s role as a destination for Latin American capital—considered to be illicit financial flows—has been documented for decades. It is estimated that in 1986, 29% of all LAC capital deposited abroad was in Miami. This phenomenon is referenced in the American series Miami Vice that began airing in the mid-1980s, which showed the city as a center of money laundering, drug trafficking and arms trafficking operations.

The 80s: Looking back

The 1980s were a time of substantial reforms, especially in the structure of the economic policy of international financial flows in Latin America and the Caribbean. It was during this period that tax havens and offshore banking started becoming prominent. The phenomenon came...
What is the Preferred Banking System for Foreign Capital Deposits of Developing LAC Countries?

The geopolitical dimension has to do with the Bretton Woods agreements. After World War II, it was defined that the dollar would be the unit of account in planetary commerce. After the breakdown of Bretton Woods in 1971, the Petrodollar agreement between the Arab monarchies and the United States government was consolidated so that the oil and gas trade—main energy and raw materials for the chemical sector (e.g., fertilizers, textiles, plastic)—would be denominated in US dollars. The demand for dollars for international trade in turn generates demand for banking services with access to dollar payment systems. While the ‘xenodollar’ phenomenon (dollar accounts outside the United States) is an option, the only issuer of last resort in case of insufficient liquidity for international payments is the United States, particularly the Federal Reserve. Because dollars are created as banks’ liabilities, dollars continue their lifecycle in circulation as electronic accounting records on the balance sheets of the banks that created them. When dollars flow from one bank to another bank, records are also registered in a third ‘correspondent’ bank—as explained, generally based in the United States. It is only when dollars flow within the same bank that the records are not shared elsewhere.

Additionally, the Basel Committee on Banking Supervision has issued regulations that worsen the systematic behavior of placing capital abroad. As we have seen, two-thirds of the assets abroad of Latin America and the Caribbean are from financial institutions (including commercial banks and central banks). Therefore, it is absolutely crucial to ask why banks place their liquid assets in developed countries, particularly in the United States. A part of this liquidity is the result of international payments through exports, remittances, etc. But another part is due to portfolio optimisation decisions. According to Basel international standards, a large part of the banks’ portfolios must be invested in maximum safe and liquid securities. At the international level (primarily the US, Germany and Japan), government bonds attain maximum safety and liquidity. Although in some cases, Latin American banks directly acquire US government bonds. In others, however, they acquire stakes in money-market funds (liquid investment funds) that in turn invest in US government bonds or maintain liquid deposits in the US banking institutions that are “too big to fail” (of systemic importance, also called “megabanks”).

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When dollars flow from one bank to another bank, records are also registered in a third ‘correspondent’ bank—generally based in the United States.
The Role of Megabanks

The institutions that have been considered megabanks by Basel are listed in the table below, organised into five categories according to their global systemic importance. Nine of the twenty-nine banks are from the United States. Two of the four largest banks are from the United States. The largest bank is also from the United States. It is in these institutions where the records of illicit financial flows remain. In particular:

Only taking the activity of financial flows variables from the data used by BIS to carry out this categorisation (in 2017), 20 banks (among the 76 largest banks in the world) concentrate 68% of the activity of financial flows. The statistics refer only to payments ordered by those institutions through high value payment systems excluding intra-group payments. Six of these banks, almost all of them from the United States, (JP Morgan, BNY Mellon, Citigroup, Deutsche Bank, Bank of America and HSBC) concentrate 39% of the payment activity. On its own, JP Morgan concentrates 12% of the payment activity of 76 large banks worldwide; its payment activity was EUR 242.8 billion in 2017.

Figure 6: Globally Systemically Important Banks
(from highest to lowest importance)

<table>
<thead>
<tr>
<th>Category</th>
<th>Megabanks</th>
</tr>
</thead>
<tbody>
<tr>
<td>5</td>
<td>(empty)</td>
</tr>
<tr>
<td>4</td>
<td>JP Morgan Chase</td>
</tr>
<tr>
<td>3</td>
<td>Citigroup, Deutsche Bank, HSBC</td>
</tr>
</tbody>
</table>

Among the Wolfsberg Group’s priorities for 2019 are “reducing friction for the customer” and “ensuring data privacy guarantees”. This means that they continue to promote the free transfer of financial flows and bank secrecy.

The level of interconnectedness between banks is measured by the amount of liabilities they have with other each other. In this category, 20 banks (including seven in China) account for 52% of intra-bank liabilities. Six banks concentrate 19% of intra-bank liabilities: JP Morgan, Deutsche Bank, Industrial Commercial Bank of China, Mitsubishi UFG, HSBC and Shanghai Pudong. At the end of 2017, JP Morgan led the concentration of intra-bank liabilities with EUR 350 billion, which represented 4% of this category.

In relation to cross-border liabilities- a proxy for their role in international correspondent networks, including non-resident direct clients - 20 banks (of the 76 largest in the world) concentrate the 65%. Six banks (HSBC, BNP Paribas, Santander, Citigroup, ING Bank, JP Morgan) concentrate 30% of cross-border liabilities. The HSBC, from the United Kingdom, leads this category with 7% of cross-border liabilities of the 76 largest banks in the world; in total, it registered EUR 116 billion at the end of fiscal year 2017.

In the public sphere, Senator Carl Levin of the United States has carried out multiple investigations on the role of US banks in the systemic facilitation of illicit financial flows. Megabanks have been evidenced as systemic facilitators of IFFs-sometimes as direct promoters of such flows and other times as a result of negligence or as passive actors of international flows.

Aware of the systemic role they play in illicit financial flows, the largest Western banks (including Japan) formed the Wolfsberg Group. It is a group of thirteen megabanks (see figure 7) dedicated to developing frameworks and guidance for financial crime risk management, from a banking perspective. Among the group’s priorities for 2019 are “reducing friction for the customer” and “ensuring data privacy guarantees”. This means that they continue to promote the free transfer of financial flows and bank secrecy. Next is the composition of group members. They are the same institutions that star in the list of megabanks and serve as systemic facilitators of illicit financial flows, revealed through self-selection.

Figure 7: Transnational megabanks members of the Wolfsberg Group (June 2019)
Residents in Mexico accumulate $118 billion in banks abroad. Of that amount, $50 billion correspond to capital of the non-banking sector and $42 billion of the non-financial sector. As can be seen in the graph, the tendency to accumulate assets abroad is increasing, especially since 1994, when the North American Free Trade Agreement (NAFTA) came into effect.

Mexico places its capital primarily in the United States. This is not in vain; Mexico is one of the few countries in the world that has had, in the past, a swap line with the United States Federal Reserve and currently has a swap line with the United States Department of the Treasury. Undoubtedly, due to the geographical proximity and the deep economic and financial ties between Mexico and the United States, the US has become the main destination of Mexican financial flows. The US accounts for 61% of total deposits of Mexican residents and 79% of non-

Figure 8: Deposits of Mexican residents in Foreign Banks (1977-2018, USD thousands)

Source: Locational Banking Statistics, Banco de Pagos Internacionales (BIS)
Due to their geographical proximity, and their deep economic and financial ties, the United States accounts for 61% of total deposits of Mexican residents and 71% of non-banking sector deposits. Only 6% of Mexico’s deposits abroad seem to be in jurisdictions that prefer to keep the BIS statistical disaggregation by country confidential.

It is worth examining the deposits in the US. It is often overlooked that the US jurisdiction allows a certain amount of relaxation in regulatory treatments, especially for the creation of certain corporations or foundations. While the BIS reports $71.6 billion of Mexico’s deposits in the US, the US TIC reports $79.6 billion. On the non-bank side, the BIS reports $35.6 billion and the US TIC reports $33.8 billion. Both figures approximate each other, thus are considered within a range of statistical tolerance. Detailed figures by type of deposit instrument reveal that the non-banking sector (companies and individuals) have a strong presence in the United States. Deposits in the US amount to approximately 25% of all deposits in the Mexican banking system.

It is a research challenge to identify which would be the main US banks that receive the deposits of Mexican residents in order to investigate illicit financial flows of Mexican origin channeled through US banks.

Wolfsberg Banks in Mexico

Mexico has a large presence of foreign financial entities in its territory. Credit Suisse, JP Morgan, Citigroup, Santander, Bank of America, Barclays, Deutsche Bank, HSBC, MUFG are entities that make up the Wolfsberg Group and operate in Mexico under multiple banking licenses. Société Générale has a representative

**Figure 9: Deposits of Mexican residents in foreign banks, by country (to December 2018)**

<table>
<thead>
<tr>
<th>Deposits by country</th>
<th>Total (USD billions)</th>
<th>% of total</th>
<th>Non-banking (USD billions)</th>
<th>% of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>US: United States</td>
<td>71.6</td>
<td>58.8%</td>
<td>35.6</td>
<td>21.9%</td>
</tr>
<tr>
<td>ES: Spain</td>
<td>7.7</td>
<td>6.5%</td>
<td>2.7</td>
<td>5.3%</td>
</tr>
<tr>
<td>CH: Switzerland</td>
<td>7.6</td>
<td>6.4%</td>
<td>3.4</td>
<td>6.8%</td>
</tr>
<tr>
<td>CA: Canada</td>
<td>4.7</td>
<td>4.0%</td>
<td>0.8</td>
<td>1.6%</td>
</tr>
<tr>
<td>GB: United Kingdom</td>
<td>4.6</td>
<td>3.9%</td>
<td>1.9</td>
<td>3.7%</td>
</tr>
<tr>
<td>Others</td>
<td>3.5</td>
<td>2.9%</td>
<td>7.0</td>
<td>12.9%</td>
</tr>
<tr>
<td>Unknown</td>
<td>18.2</td>
<td>15.4%</td>
<td>5.8</td>
<td>11.5%</td>
</tr>
</tbody>
</table>

Source: Locational Banking Statistics, Banco de Pagos Internacionales (BIS)

**Figure 10: Deposits of Mexico residents in US banks (to December 2018)**

<table>
<thead>
<tr>
<th>Deposits in US</th>
<th>USD billion</th>
</tr>
</thead>
<tbody>
<tr>
<td>TOTAL</td>
<td>79.6</td>
</tr>
<tr>
<td>Payable in dollars</td>
<td>72.5</td>
</tr>
<tr>
<td>Total own liabilities payable in dollars</td>
<td>64.0</td>
</tr>
<tr>
<td>Total custory liabilities payable in dollars</td>
<td>8.5</td>
</tr>
<tr>
<td>Non negotiable deposits Held by foreign official institutions and foreign banks</td>
<td>30.4</td>
</tr>
<tr>
<td>Non negotiable deposits Held by all other foreigners</td>
<td>27.5</td>
</tr>
<tr>
<td>Negotiable CDs Held by foreign official institutions and foreign banks</td>
<td>3.4</td>
</tr>
<tr>
<td>Negotiable CDs Held by all other foreigners</td>
<td>5.0</td>
</tr>
<tr>
<td>Other liabilities Held by foreign official institutions and foreign banks</td>
<td>4.9</td>
</tr>
<tr>
<td>Other liabilities Held by all other foreigners</td>
<td>1.3</td>
</tr>
<tr>
<td>Total liabilities payable in foreign currencies</td>
<td>7.1</td>
</tr>
</tbody>
</table>

office and UBS operates as a brokerage and wealth management firm (investment advisor).

Bank of China, Industrial and Commercial Bank of China (ICBC) and Mizuho are not in the Wolfsberg Group but are part of the megabank list. They also operate in Mexico. However, it is noteworthy that Bank of China, Barclays, Deutsche Bank, Mizuho and ICBC (in that order) have zero or negligible levels of deposits in the Mexican jurisdiction. These institutions, in addition to the operations of Société Générale and UBS, should be flagged as possible regulatory arbitrage practices. These entities could be taking advantage of their

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**Figure 11: Deposits in Banks Operating in Mexico**

(end-December 2018)

<table>
<thead>
<tr>
<th>Deposits by Banks**</th>
<th>MXN million</th>
<th>Share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>BBVA Bancomer</td>
<td>1,218,560</td>
<td>21.3%</td>
</tr>
<tr>
<td>Banorte</td>
<td>792,391</td>
<td>13.8%</td>
</tr>
<tr>
<td>Santander</td>
<td>775,840</td>
<td>13.6%</td>
</tr>
<tr>
<td>Banamex (Citigroup)</td>
<td>678,574</td>
<td>13.4%</td>
</tr>
<tr>
<td>HSBC</td>
<td>464,209</td>
<td>8.1%</td>
</tr>
<tr>
<td>Scotiabank</td>
<td>385,791</td>
<td>6.7%</td>
</tr>
<tr>
<td>Inbursa</td>
<td>236,756</td>
<td>4.1%</td>
</tr>
<tr>
<td>Banco del Bajo</td>
<td>166,215</td>
<td>2.9%</td>
</tr>
<tr>
<td>Banco Azteca</td>
<td>123,665</td>
<td>2.2%</td>
</tr>
<tr>
<td>Banregio</td>
<td>94,624</td>
<td>1.7%</td>
</tr>
<tr>
<td>Multiva</td>
<td>86,256</td>
<td>1.5%</td>
</tr>
<tr>
<td>Bancoppel</td>
<td>56,562</td>
<td>1.0%</td>
</tr>
<tr>
<td>Afemex</td>
<td>53,696</td>
<td>0.9%</td>
</tr>
<tr>
<td>Monex</td>
<td>45,644</td>
<td>0.8%</td>
</tr>
</tbody>
</table>

Banco Mifel 45,104 0.8%
Sabadell 42,662 0.7%
Ve por Más 40,436 0.7%
CIBanco 32,728 0.6%
Banco Ahorro Famsa 30,880 0.5%
Actinver 26,514 0.5%
Bank of America 25,116 0.4%
Invex 24,492 0.4%
MUFG Bank 22,209 0.4%
J.P. Morgan 19,530 0.3%
Compartamos 18,889 0.3%
Banco Base 16,445 0.3%
Credit Suisse 15,067 0.3%
Intercam Banco 15,031 0.3%
Bansí 13,632 0.2%
Bancrea 11,835 0.2%
American Express 10,297 0.2%
ABC Capital 6,180 0.1%
Consobanco 5,867 0.1%
Inmobiliario Mexicano 5,659 0.1%
Autofin 5,156 0.1%
Accendo Banco 4,245 0.1%
ICBC 3,787 0.1%
Mizuho Bank 3,365 0.1%
Finterra 3,278 0.1%
Volkswagen Bank 2,679 0.0%
Banco S3 1,167 0.0%
Shinhan 481 0.0%
commercial presence—physical establishments—but orienting their deposit-taking business to their subsidiaries in other jurisdictions outside the Mexican territory. In some countries, the deposit-taking by entities that do not have a domestic bank license carries penalties of a criminal nature. Additionally, such uptake would be incurred in the cross-border mode of financial services under the General Agreement on Trade in Services, which were not necessarily included as commitments to liberalisation.

Mexican banks in offshore jurisdictions

On the other hand, it has been possible to identify two Mexican private banks operating in offshore banking jurisdictions. The first is Banco Azteca, in Panama. According to the Superintendence of Banks of Panama, this operation has deposits for $21.6 million, which are 100% from Panamanian clients. Additionally, credit operations are 97% within Panama. Banco Azteca has 393 employees in six physical branches in Panamanian territory.

The second is Banorte, in the Cayman Islands. Besides the fact that it has a type B banking license (no physical presence required), there is no more information available on them. Although, the Cayman Islands Monetary Authority (CIMA) argues that banks with a type B banking license are subject to consolidated supervision by the national supervisory authority—in this case, the Mexican National Banking and Securities Commission (CNBV)—no publicly available document of consolidated supervision agreements was found between CNBV and CIMA.

Additionally, Mexican state-owned banks Nacional Financiera and Banco de Comercio Exterior have branches in the Cayman Islands with type B licenses (no physical presence required). In addition to the megabanks identified above, BBVA and Scotiabank also have an offshore presence, particularly in the Cayman Islands. In the case of BBVA, in addition to a bank license in Cayman Islands, it also has a license for the administration of trusts. The administration of trusts is a tool used more as a facilitator of illicit financial flows to add one more level of secrecy and legal veil to the final beneficiary.
The Case of Cayman Islands

The Cayman Islands are the most transnationalised offshore banking jurisdiction. Only 2% of deposits in banks domiciled in the Islands are from capital originating there. These Islands, located in the Caribbean, fulfill a systemic function in The United States’ financial system and therefore in the global financial system. However, it also has a broad history of illicit financial flows with Latin America.

The US TIC reports approximately $5440 billion deposits and short-term securities (including Treasury bonds) from abroad (June, 2018). With $1513 billion, the Cayman Islands are, in turn, the largest depositor in the US banking system. To understand the magnitude, it is worth comparing this amount with those of other countries. The Cayman Islands’ funds in the US are 1.5 times larger than those of the United Kingdom, almost four times larger than those of Japan and 10 times larger than those of China. The Cayman Islands, alone, account for 25% of all short-term cross-border liabilities of the US banking system. This data is explained by the importance of “shadow banks”—financial entities without a banking license, such as investment funds or hedge funds. In many cases, this money simply serves a round-tripping function for regulatory and tax arbitrage purposes.

US shadow banks place money in the Cayman Islands to take advantage of unlimited leverage and lower solvency requirements, on the one hand, and non-existent tax rates, on the other. Considering specifically the banking sector, out of the $819 billion reported by CIMA in cross-border deposits in banks of the Cayman Islands, $446 billion are deposited in US banks. That is, half of every dollar deposited in banks in the Cayman Islands is redirected to US banks. Consequently, almost all megabanks in the world operate in the Cayman Islands.

According to the BIS, in 2011 there were 234 banks in the Cayman Islands. Till date, 133 banks are operational, almost all of them with a type B license (no physical presence required). Only ten banks have a Type A license (which allows them to operate with local customers). In type B banks, 265 people work in the Islands and 3285 people work outside the Islands. The reduction in the number of offshore banks, according to CIMA, is attributed to Regulation Q of the Dodd-Frank banking regulation legislation in the United States. This regulation allowed banks to remunerate liquid deposits in US banks with interest. However, the requirements of other regulation put in place to prevent money laundering and help combat the financing of terrorism increased transaction costs for banks.
operating in offshore jurisdictions. Not only have banks been shut down (as is evident in the case of the Cayman Islands) but also, according to the BIS, correspondent relations between onshore and offshore banks have been severed. In the case of the Cayman Islands, between 2012 and 2018, 21% of bank correspondent relationships (bank accounts in other banks) have been closed. According to the CIMA, there are 20 banks from Central America and the Caribbean, 15 banks from Canada and Mexico and 34 banks from South America operating in the Islands. This shows the deep relationship that exists between Latin American banks and the jurisdiction.

CIMA reports that $50.6 billion in developing Latin America and Caribbean are deposited in the Cayman Islands. The vast majority correspond to deposits from the banking sector. In fact, 68.5% of all deposits in the Islands correspond to intra-group deposits of the banks mentioned. Only 31.5% corresponds to deposits from other sectors. This shows the concentration of deposits in the banking sector.

Figure 12: National origin of Banks licensed to operate in the Cayman Islands

Figure 13: Banks of Latin America in Cayman Islands (June 2019)

TYPE OF LICENSE: BANKING
Banco ABC Brasil S.A.
Banco Bradesco S.A.
Banco do Brasil S.A.
Banco do Estado do Rio Grande do Sul S.A.
Banco Mercantil del Norte, S.A., Institución de Banca Múltiple, Grupo Financiero Banorte
Banco Mercantil do Brasil S.A.
Banco Nacional de Comercio Exterior, SNC
Banco Sumitomo Mitsui Brasileiro S.A.
Bancolombia Cayman
BCP Finance Bank, Ltd.
Itaú Banco de Investimento do Brasil S.A.
Itaú Unibanco Holding S.A.
ITAU UNIBANCO S.A.
Mizuho do Brasil Cayman Limited
Nacional Financiera S.N.C.
St. Georges Bank & Trust Company (Cayman) Ltd.
Venezolano De Credito, S.A., Banco Universal

TYPE OF LICENSE: BANKING & TRUST
Atlantic Security Bank
Banco BTG Pactual S.A.
Itaú Bank & Trust Cayman Ltd.
Itaú Bank, Ltd.
Mercantil Bank and Trust Limited (Cayman)
$7.5 billion belong to the non-banking sector of developing Latin America and the Caribbean.

**Banks of Latin America in Cayman Islands**

Given that CIMA does not publish detailed information on each bank, an initial approach was made to determine, through secondary sources, the nationality of the banks that are domiciled in the Cayman Islands that could be of Latin American or Caribbean origin. It can be concluded that Brazilian banks have a very strong presence in this jurisdiction.

To understand the role of banks as facilitators of illicit financial flows, we can look at two specific cases: the HSBC with headquarters in London, United Kingdom and the Atlantic Security Bank of the Cayman Islands.

**HSBC**

HSBC has been at the center of media and judicial attention on a recurring basis for its role as a facilitator of illicit financial flows. In fact, it has operations in the Cayman Islands and Panama, two offshore centers. Its main activities are administration of trusts, private banking and institutional banking services. Private banking or wealth management is a term used when catering to wealthy clients.

**Atlantic Security Bank (ASB)**

The ASB is an offshore bank, with a type B license, in the Cayman Islands. This means that it does not require a physical presence in the Cayman Islands. In fact, it reports its main offices in Lima, Peru and indicates that almost all of its clients are located in Peru. ASB is a subsidiary of the Peruvian financial group Credicorp (Banco de Crédito del Perú - BCP) and reports that it has operations in the Cayman Islands and Panama, two offshore centers. Its main activities are administration of trusts, private banking and institutional banking services. Private banking or wealth management is a term used when catering to wealthy clients.

According to the information reported by Credicorp (which is established in the offshore jurisdiction of Bermuda) to the Securities and Exchange Commission (SEC), the ASB has 136 employees. The group reports 34 thousand employees in the Hemisphere.

The main shareholder of Credicorp Ltd.– in Bermuda– is Dionisio Romero Paoletti. Unconventionally, one of the main shareholders of Credicorp Ltd. is Atlantic Security Holding Corporation, which is, in turn, a subsidiary of Credicorp Ltd. Additionally, the offshore bank in the Cayman Islands, Atlantic Security Bank, is the custodian of a portion of the Credicorp shares.

Atlantic Security Bank is in lawsuits in the courts of New York and the British Virgin Islands, with the successor fund of American scammer Bernie Madoff, which claims about $120 million from ASB.

ASB has been involved in more than one irregular operation. A former director of the Lima Drinking Water Service (SEDAPAL) had transferred $409,000, possibly due to bribes, from an account in the BCP to the ASB®. In this case, even though the press narrated the story as if the money had travelled to a distant bank in the Cayman Islands, it was actually a book transaction between the Peruvian bank and its subsidiary. It is not clear which of the two banks served as the correspondent of the other, but it is striking that both banks have not performed the due diligence of a director of a public institution.
Figure 14: Corporative Credicorp Ltd. Corporate structure (to March 2019)

The Case of Cayman Islands

The former Peruvian president, Pedro Pablo Kuczynsky denied making transfers between the ASB and the BCP, in 2006, for $695,000. However, the Investigative Commission of the Peruvian Parliament obtained evidence of various transactions. The Commission argued that the transfers were caused by bribes from Odebrecht. Again, the role of the BCP as a facilitator of transfers, both to and from the ASB is evident, since in reality they are transfers within the same group²⁹.

In addition, the BCP has confirmed that both transfers were made under order of Dorado LTD and the issuing bank in-charge was the Atlantic Security Bank (ASB) located in the Cayman Islands. It should be noted that Mr. Kuczynski Godard expressly denied such transfers, despite the fact that the members of the Commission consulted him twice on the origin of the $695,000 that he “paid” Golden LTD. It should be noted that the ASB is an entity that belongs to Credicorp, therefore this bank and the BCP belong to the same economic group.

Excerpt from the report of the Investigative Commission of the Congress of Peru

<table>
<thead>
<tr>
<th>Fecha de Emisión</th>
<th>Importe Dolares</th>
<th>Referencia del Remitente</th>
<th>Ordenante</th>
<th>Cuenta Destino</th>
<th>Beneficiario</th>
<th>N Operacion</th>
</tr>
</thead>
<tbody>
<tr>
<td>15/03/2006</td>
<td>3,50,000.00</td>
<td>TRE10106093281</td>
<td>ATSEKYKY</td>
<td>1.93101E+12</td>
<td>Pedro Pablo Kuczynski Y/O Gloria Jesus Kisic</td>
<td>STB42231</td>
</tr>
<tr>
<td>22/03/2006</td>
<td>3,45,000.00</td>
<td>TRE10106093974</td>
<td>ATSEKYKY</td>
<td>1.93101E+12</td>
<td>Pedro Pablo Kuczynski Y/O Gloria Jesus Kisic</td>
<td>STB63615</td>
</tr>
</tbody>
</table>

Fuente: Carta N° R - 7579049-1 del BCP


18 United States Treasury Information Capital


22 Round-tripping is when funds are paid abroad and re-placed in the country of origin as FDI. The goal is to appear as if it were to be investment, but it is not. This is facilitated by US and European tax havens. [online] Available at: https://documentos.memoriayciudadania.org/ [Accessed 18 Dec. 2019].


How to Use the Toolkit?

The toolkit is as an easy and accessible resource for enthusiasts, activists, civil society organisations, practitioners and journalists. Designed in a modular format, the toolkit aims to enable evidence based advocacy from the perspective of developing countries for bringing awareness, policy change, exchanging examples of effective interventions from the Global South and wider collaboration between different actors. Please note that the policy recommendations are aimed to be adapted and tailored across settings, regions and priorities.

All modules are designed independently from each other but are structured in a holistic manner. It is recommended that Module 1 be read first as it sets the premise for this undertaking. The toolkit fulfills three objectives -

提供了全面的视角，了解非法金融流出的全球南方语境及其区域成分。

引介了一系列在人权、性别正义和可持续发展目标框架下进行人权侵害和解决非法金融流出影响的术语。

通过国际和地区机制、简化案例研究和全球南方成功干预的示例，使用多管齐下的方法来动员更大的民间社会、实践者和记者。

The toolkit is available in print and online. The technical module is available in Spanish.

A Toolkit on Illicit Financial Flows: Perspectives from the South

Module 1: Politics of Defining IFFs
Module 2: IFFs and the Extractives Section in Asia
Module 3: Advocacy Manual for Lawyers’ Association in the Global South
Module 4: Addressing Illicit Financial Flows – National, Regional and Global Interventions
Module 5: Technical module: The Role of Banking in Latin America as a facilitator of Illicit Financial Flows

1 This toolkit uses the terms developing countries or regions interchangeably with the Global South. The term ‘Global South’ represents countries in the developing regions of Africa, Asia and Latin America, Central America, Mexico, South America, and the Middle east (with the exception of Israel), Japan, Hong Kong, Macau, Singapore, South Korea and Taiwan). Southern countries refer to countries belonging to the Global South.
About Financial Transparency Coalition

The Financial Transparency Coalition (FTC) is a global civil society network working to curtail illicit financial flows through the promotion of a transparent, accountable and sustainable financial system that works for everyone. For more information, kindly visit: https://financialtransparency.org/