Understanding the Global Data on Illicit Financial Flows: A Legal Perspective.
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Executive Summary
Due to the increased attention given to Illicit Financial Flows (IFFs) globally, the data provided to support its magnitude is having repercussions across industries, sectors and stakeholders. The regulation, control and eradication of IFFs as a result has gained importance. However, there remains controversy on the data and questions exist on its reliability. This policy brief will explore the statistics given on IFFs globally, the diverse critiques that have been floated and the validity of the data from a legal perspective as well as making recommendations on how to approach the data.

1. Introduction
The phrase ‘Illicit financial flows’ is not a legal term nonetheless; it is being used by both the legal and non-legal fraternity to describe both criminal and legal activities. It is a phrase that although recently coined has gotten global recognition over the past decade. It describes money ‘illegally earned, transferred or used’\. As a result, it covers: one, legally earned money that has been illegally transferred or used; or two, legally used money that has been illegally earned or transferred. It can cover both domestic or cross border transactions; private and public transactions; formal and informal transactions or a combination of any of them. However, it does not consider barter trade. It speaks of an incredibly large amount of money being unregulated at a global level with estimated figure of 1.9 trillion dollars. At the continental level, the data estimates show 100 billion flowing annually out of Africa; approximately USD 285 billion from Asia; 200 billion

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from developing European countries; 116 billion from Latin America and the Caribbean; 87 billion from the MENA region in 2011; and an estimated 1 trillion loss from Europe and North America.

If one were to look at the data on trade mispricing, the analysts’ access to the information is limited. They may look at the data but it only shows the legal transactions as registered by the data collection agencies at the ports. If for example, a person places different items from those officially declared in a cargo container there is no way of verifying this data unless the border official catches the smuggler while physically checking the container. In addition, financial data cannot be triangulated because while goods and services may move between 2 or more countries, the payments often digital may move between banking institutions in a completely different set of states.

Two issues arise from a legal perspective: one, the veracity of the data and two, the underlying legal problems in stopping, tracking and returning these flows to their rightful destination. This policy brief highlights the diversity in the data. Despite the diversity of positions, this brief will move forward on the ground that these debates do not detract from the legal, economic and fiscal policy considerations that all states globally should consider when implementing reforms jointly and

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separately while relying on this data. This paper is divided into 4 parts: one, unpacking the definition and the data connecting to it; two, unpacking the data and pointing to both its strengths and weaknesses and three, making recommendations on the use of this data as well as how to improve it before finally, concluding.

2. The Legal Problems
2.1. Defining Illicit Financial Flows
Illicit money can be classified into three main forms:

- The proceeds of theft, bribery and other forms of corruption by government officials;
- The proceeds of criminal activities including drug trading, racketeering, counterfeiting, contraband, and terrorist financing;
- The proceeds of tax evasion and laundered commercial transactions\(^3\).

Although there is a debate on the definition, no matter which way one looks at it, the above three parameters are not in debate. Nevertheless, while creating these 3 classes within the definition the grouping by its very nature does not take into consideration the laws of different countries. For example, what is considered a bribe under the United Nations Convention against Corruption\(^4\) may be different in the domestic laws of individual countries. In the case of commercial corruption surrounding the world, football federation (FIFA) often referred to as the ‘bribery case with no bribery charge’ as there is no law on how money can be moved commercially by non-government institutions the collusion between the FIFA officials in commercial transactions could not raise a criminal charge of bribery.\(^5\)

In other instances, although there are laws, there is limited, little or no enforcement e.g. Austria, Canada, Finland, Singapore, India, Mexico\(^6\) this means that data on these examples would be excluded from some IFF estimates.

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In 2001, Anti-bribery legislation to implement the 1997 OECD Anti-Bribery Convention became effective in Netherlands. This means that the data from the Netherlands would not have included these amounts as an IFF. This concern of what is legal and illegal in different countries is an overarching problem which most of those working on the economic estimates have not yet addressed.

The IFF definition is set out as deliberately wide as it is intended to include both legal and illegal activities. For example, transfer mispricing is illegal only in countries where there is a law on transfer pricing. This law on transfer pricing allows a subsidiary company to move goods and services to another subsidiary or its parent company (a related company) at cost that as a result does not register a profit and therefore does not attract taxation. In addition, not all countries in the world have laws on transfer pricing and even when the law exists, it may not have the requisite regulations. The EY Worldwide Transfer Pricing Reference Guide 2018-2019 only covers 124 jurisdictions or 102 countries out of 199 countries globally.

2.2. Evidence Law and IFF
Different countries globally have different thresholds for what information has evidentiary value in their judiciaries, their legislatures or their executives. One of the first analyses of IFF data came from GFI and included analysis of trade misinvoicing. The collection and transmission of this information can be traced from customs officials filing in national customs databases, after which the data is transmitted to the government data and statistics offices, and later on to global data repositories, international institutions and financial bodies. This country data is then cross-referenced with the corresponding countries by institutions who then estimated the IFF through misinvoicing using data transmitted electronically. Meso data like this as it is compiled often receives challenges on veracity and reliability.

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Within legislatures and executives, data of this nature is often presented by different stakeholders in guiding the legislation and policies being recommended for adoption in any sub-national, national, regional, continental or global parliaments and governments. However, the data is treated as persuasive at best and a guide for thinking and debate that results in law and policy making that is a reflection of the thinking of the majority. Conversely, depending on the stakeholder(s) that present the information it will be either be taken on board or rejected and tends to be susceptible to lobbying processes.

Within judiciaries (national or international), rules of evidence guide the manner in which data is presented and relied upon. For example in the US federal rules of evidence rule 902 the admissibility of documents from electronic sources states that an adverse party must have reasonable written notice and a fair opportunity to challenge it. A false foreign record attracts a criminal penalty in the country where the certification is signed. In addition, only a qualified person can give certification of accuracy for electronically generated records. In addition, when admitting a document in a civil court as evidence, rule 36 of the US federal rules of civil procedure highlights that a party may request that an opponent admit the 'genuineness of a document' but authentication is not all that matters in admissibility of web based evidence, the information may be authentic but cannot be used to establish a prima facie case as was highlighted in Doe v. Flaherty. The data highlighting illicit financial flows even if admissible in a court of law is not strong enough evidence to establish a prima facie case even when authenticated.

3. Understanding the Data
As at 2019, the IFF data available includes analysis estimating trade mispricing: criminal activity and corruption. Nevertheless, there are no estimates presently available on one, linking money movements with their contracted goods and services; two, transactions purely in the digital economy; and finally, cash based informal economy transactions. In addition, the data can only guess at the size of the corruption and criminal activity since by their very nature IFFs related to

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12ibid.
13ibid.
14Doe v. Flaherty, 623 F.3d 577 (8th Cir. 2010).
criminal or illegal activities are designed to avoid regulation and oversight. The statisticians who work in specific fields focus on their particular field with the result there is limited cross discipline connections and analysis of data from the different statistical fields. For example, the analyst working on data on tax revenue losses from illicit outflows is different from one analysing data on import duties. Therefore, researchers who try to analyse the entirety of IFF face multiple hurdles. All of these result in an unreliable margin of error resulting in contradictory analysis.

3.1. Trade Mispricing Data
The first set of data to gain global recognition was the GFI data and the work of Boyce and Ndikumana which, developed IFF data based on estimates; but these were limited to trade mispricing and misinvoicing. For example, the Kenyan economy lost USD 9.64 billion in potential domestic investment from export under-invoicing and import over-invoicing during the years of 2002-2011 in this study, the government may have lost:

- USD 3.92 billion in tax revenue resulting from these illicit outflows and from the USD 3.94 billion in illicit inflows\textsuperscript{15}.
- Tax and tariff revenues of USD 3.92 billion over the course of this study or an average of USD 435 million per year, based on official tax and tariff rates\textsuperscript{16}.

The country of Mozambique lost USD 2.33 billion in illicit outflows of capital due to trade misinvoicing in the 2002-2011, which, combined with cumulative illicit inflows of USD 2.93 billion, may have denied the government USD 1.68 billion in revenue\textsuperscript{17}.

Import under-invoicing was the most rampant method of bringing in illicit capital in Mozambique, it totalled USD 2.22 billion from 2002-2010, an average of USD 247 million annually. This implies a loss in:

- Import duties of USD 37 million,
- VAT revenues at around USD 42 million,
- Corporate tax revenue equates to approximately USD 83 million on average.

This combined with the losses incurred from import under-invoicing brings the average annual tax loss estimate to approximately USD 187 million per year\textsuperscript{18}.

\textsuperscript{16}ibid.
\textsuperscript{17}ibid.
\textsuperscript{18}ibid.
These two country examples highlight a figure much smaller than what is taking place on the ground. In Kenya, for example the revenue authority due to poor laws and regulations repeatedly lost transfer-pricing cases. In Mozambique, huge amounts of money have been channelled into corporations led by political elites. Both case studies while pointing towards the problem are underestimations of the real amount of IFF.

3.2. Data on Criminal Data

Data collected globally shows the amount of illicit financial flows from the global economy shows that counterfeiting and piracy amounts to USD 461 billion in 2013$^{19}$

- On drug trafficking, the network is currently estimated to be worth between $400 and $600 billion, the illicit drug business is growing alongside licit trade hotspots with illicit trafficking of opiates to Europe yielding an estimated $28 billion annually$^{20}$.
- Illegal logging is estimated to cause tax losses for governments annually valued at approximately USD 5 billion$^{21}$
- Human trafficking is valued at USD 150 billion globally$^{22}$

However, the continental level data indicates the amount of illicit financial flows from Africa annually as varying by almost 300%. For example,

- Transnational criminal activities (counterfeiting) being USD 923 million to USD 1.13 billion has a difference of 900 million,
- Drug trafficking USD 426 billion to USD 652 billion a difference of 230 billion,
- Illegal logging USD 52 billion to USD 157 billion has a difference of 105 billion,
- Human trafficking USD 150.2 billion,
- Illegal wildlife trade USD 5 billion to USD 23 billion has a difference of 18 billion

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• Small arms and light weapons trafficking USD 1.7 billion to USD 3.5 billion, (In Libya, sale of arms, even though done publicly tracking the online sale of arms is challenging, particularly given the borderless nature of the trade\(^\text{23}\)) has a difference of 1.8 billion,

• Trafficking in cultural property USD 1.2 billion to USD 1.6 billion has a difference of 0.4 billion; totalling between USD 1.6 trillion to USD 2.2 trillion\(^\text{24}\) with a difference of 0.6 trillion.

### 3.3. Data on Corruption

Additional disparities on corruption data shows that while on the one hand it was reported that USD 2 trillion is lost on corruption annually\(^\text{25}\) another source stated that money lost on corruption is estimated between USD 1.5 trillion to USD 2 trillion\(^\text{26}\). The EU alone losses €179 billion and €990 billion every year to corruption\(^\text{27}\).

### Recommendations and Conclusion

IFF should be recognised as a global problem requiring a global solution whose data seems to be underestimated rather than overestimated

1. Law on data collection and freedom of information should be improved to increase quality of data
2. All transaction data should be available to government and data collection agencies
3. Clearer and more specific laws on the financial benefits of corruption and other criminal activity as well as other IFF related legislation
4. Enforcement agencies must work more closely to pass across data on potential criminal activity to reduce data discrepancies

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5. Bureaus of statistics should work more closely with revenue agencies, banks and other financial institutions, sub nationally, nationally, regionally, continentally and globally

6. Data should be publicly available to allow for checks and balances

7. Countries should have multi-disciplinary task forces to combat illicit financial flows and enhance the collection of valid and reliable data.

In conclusion, despite the clear concerns with the data it continues to require action to be tracked, controlled and stopped.

References


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