**Conference on Improving Domestic Resource Mobilization and Stemming Illicit Financial Flows**

**Venue: Crowne Plaza Hotel, Upper Hill, Nairobi, Kenya**

**Module 1, 12 March 2019: Empirical Evidence**

**Panel 3: Trade Misinvoicing as part of IFFs**

Panelist 1

**Dr. Tom Cardamone, Managing Director, Global Financial Integrity (GFI), Washington DC, USA: Complementary information from other parts of Africa**

1. BACKGROUND

Four Primary Sources of IFFs

* Income Tax Evasion by MNCs
* Transnational Crime
* Corruption
* Trade Misinvoicing: Trade misinvoicing is the purposeful misrepresentation of value, quality or quantity of goods being imported or exported in order to evade taxes and duties

Four Primary Methods of Moving IFFs

* Profit Shifting by MNCs
* Wire Transfers using Anonymous Shell Corps.
* “Leakages” from Balance of Payments (i.e. stealing from government accounts)
* Trade Misinvoicing

Note: Trade misinvoicing is both a source of IFFs and a method of moving IFFs.

Three Things to Keep in Mind are: Trade Misinvoicing (TM):

* TM estimated to be about $1 trillion annually for all developing and emerging market countries
* Problem is severe and chronic
* No developing or emerging market country is immune from trade misinvoicing

2. SOBERING NUMBERS

GFI publishes a global estimate of TM each year. One metric used to assess the impact on the economy is the percentage of a country’s total trade with advanced economies that is misinvoiced. The global average is 18%. Here are the percentages for a select group of African nations:

Burundi – 21.2%

Namibia – 21.7%

Mozambique – 23.2%

Ethiopia – 29.3%

Botswana – 31.8%

Trade misinvocing is a severe problem in Africa. Commissioners General of Customs Departments in three African nations have told GFI that 80% of trade invoices are fraudulent.

Kenya’s TM data is as follows (from 2013 UN Comtrade data):

* Percentage of trade with advanced economies that is misinvoiced is 23%
* In 2013 Kenya lost $900 million in revenue due to TM
* This does not include $9.5 billion in trade transactions that have no corresponding import or export (i.e. orphan transactions)
* Products that are most often misinvoiced include: mineral fuels, cereal products, vehicles and used clothing
* Trade partner countries that often are involved in misinvoicing are China and India

3. REASON FOR OPTIMISM

The Kenyan government (no government) needs to wait for the international community to agree to a new global tax regime to attack its TM problem. They can take the following steps immediately:

* Law – Make TM illegal
* Regulation – Institute public beneficial ownership registries
* Policy – Create whole-of-government teams to address TM and IFFs
* Technology – have the Customs Department implement a trade risk-assessment database to identify TM while the goods are still in the port so that the proper amount of duty and VAT can be collected

Global Financial Integrity has such a trade database called GFTrade. One client government identified $100 million in underinvoiced imports in one 12-week period in 2018. GFTrade is fit for purpose and can be a game-changer for governments seeks to collect more domestic resources.

Panelist 2

**Dr. Maximilian Mainza, Head, Economics Department, Copperbelt University, Kitwe Zambia: a complementary view from Zambia**

TRADE MISINVOICING: A ZAMBIAN PERSPECTIVE (COPPER MINING)

Import and export misinvoicing data: involves overinvoicing or underinvoicing due to various reasons such as to get VAT refund and to evade taxes.

Import overinvoicing is 89% while underinvoicing is only 11% of the import misinvoicing of copper trade. 79% of import overinvoicing is from South Africa and 21% from Australia. 100% of import underinvoicing is from South Africa.

Export overinvoicing is 45% while underinvoicing is only 55% of the export misinvoicing of copper trade. 66% of export overinvoicing is to China, 25% to India, 7% to Namibia and 2% to South Africa. 31% of export overinvoicing is to China, 28% to India, 20% to Netherlands, 13% to South Africa and 8% to Germany.

Mineral royalty is a percentage based on the prices determined by the mining companies.

Hidden trade: Trade data reported as export but not reported as import by the partner country. $883.7 million in Switzerland, 12B in Congo DRC.

CONSEQUENCES

* Revenue loss
* Slowed economic growth
* Reduced investments
* Reduced employment opportunities
* Increased income inequalities

RECOMMENDATIONS

* Need for inclusive policy making to tackle the trade misinvoicing.
* Improve trade data collection.

Panelist 3

**Elsy Sainna, Deputy Executive Director of International Commission of Jurists, Nairobi**

WHY REDUCTION OF ILLICIT FINANCIAL FLOWS THAT FUELS SOUTH SUDAN’S WAR ECONOMY IS IN KENYA AND UGANDA’S INTEREST

South Sudan is ranked as a fragile state and one of the most corrupt in the world. • The policy brief by IEA traces institutional weaknesses that allow for illicit financial flows from South Sudan. • Kenya and Uganda are key destinations and/or transit points of illicit financial flows from South Sudan.

ESTIMATES OF THE SCALE AND MAGNITUDE OF IFF OUTFLOWS FROM SOUTH SUDAN TO KENYA AND UGANDA

* Manipulation of currency exchange control system in South Sudan,
* Theft of resources from extractive sector:
* Mismanagement of government

EFFECTS OF IFFS

* Disorientates the public spending e.g. education, health care
* Destabilizes the economy
* High public debt
* State capture by the elites

RISKS POSED TO KENYA AND UGANDA BY IFFS FROM SOUTH SUDAN

* Risk of international down-grading due noncompliance with local and international anti-money laundering law (AML) laws
* Risks to status of Kenya as an International Financial Centre due to complicity of state organs on dealing with IFFs from South Sudan and protection of persons under watch list.
* Sectorial distortions mainly in the real property and foreign exchange services where most of the monies from IFF end up
* Illicit financial flows weaken states and undermine effectiveness of regional bodies by compromising institutions charged with IFFs through bribery and corruption.
* Undermining foreign policy goals, especially regional peace and security, and thus eroding their contribution to the peace process in South Sudan, where they have been key players.
* IFFs may delay admission into the Egmont Group, where both countries are candidate members and thereby justifying their classification as weak AML jurisdictions by Financial Action Task Force (FATF) styled bodies..

RECOMMENDATION

* Comply with UNSC sanctions placed on individuals aiding or taking part in IFFs.
* Comply with international supervisory standards
* Information sharing
* Enforce anti money laundering laws
* Parliament to strengthen its oversight roles of combating IFFs
* Undertake risk assessments of illicit financial flows periodically and involve stakeholders in giving solutions.