NO EASY TASK:

Quantifying Illicit Financial Flows

The Financial Transparency Coalition works to curtail the whole range of illicit financial flows. Some FTC members focus on the cross-border movement of money that is illegally earned, transferred, or utilized. These illicit financial flows come from tax evasion, trade manipulation, organized crime, and corrupt payments to public officials. Coalition members also address the wider aspects of illicit flows, including tax avoidance by multinational companies.

But pinpointing the scale of the problem is no easy task. Whether it's using data to uncover trade misinvoicing, measuring the amount wealthy elites hide in secrecy jurisdictions, or quantifying how much corporations shift in profits to avoid tax, there's a growing body of literature around illicit financial flows. No matter how you look at the data, one thing is clear: financial secrecy has turned illicit flows into a thriving business.

HOW DO YOU QUANTIFY ILLICIT FINANCIAL FLOWS?

TRADE & FINANCE DATA

$7.8 TRILLION Lost By Developing And Emerging Countries To Illicit Financial Flows (2004-2013) [1]

$1.1 TRILLION Lost In 2013 Alone [1]

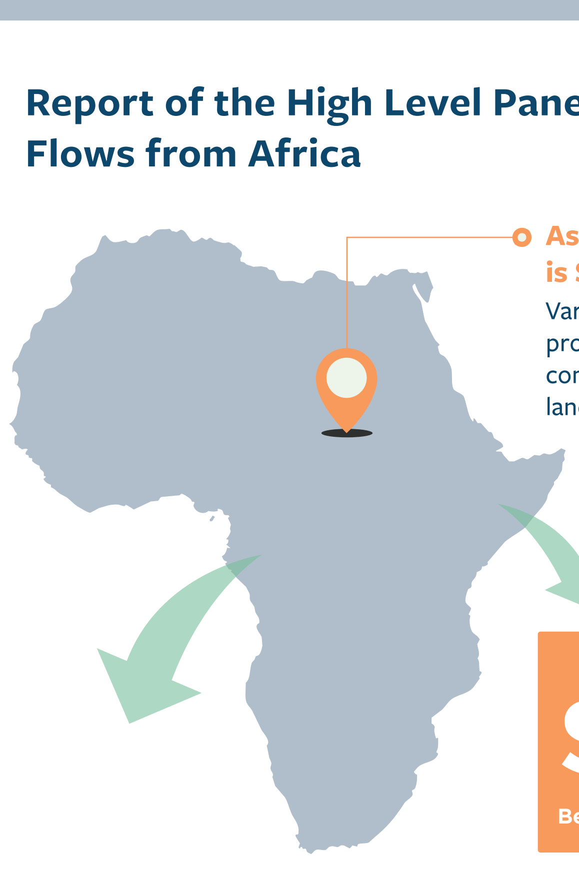
Trade misinvoicing, or moving money across borders in a commercial transaction while deliberately misreporting the value – a form of which is trade-based money laundering – is cited by Global Financial Integrity as the largest component of measurable illicit financial flows. To get to their global estimates on illicit financial flows, GFI combines the use of trade data to capture misinvoicing with an analysis of balance of payments data to identify when it looks like more money is leaving a country than what has been reported.

The Loss is Only Getting BIGGER. (* Numbers are rounded for clarity) [1]

CONSTRAINTS OF METHOD

Estimates are based on national-level trade data published by the IMF that do not permit separate identifications of price and quantity discrepancies or discrepancies in the trade of particular commodities. Missing data are often adjusted by the IMF using data from other countries. Data also does not allow for distinguishing between trade misinvoicing (unrelated parties) and transfer mispricing (related parties).

Report of the High Level Panel on Illicit Financial Flows from Africa



As a percentage of GDP, Africa is Suffering Most.

Various studies aimed at dissecting the problem in the African context have come up with staggering figures. The landmark Mbeki report found that:

* = $10 Billion

$50B Being Sucked Out Of Africa Every Year

Cumulative Illicit Financial Flows From Africa By Region [2]

CONSTRAINTS OF METHOD

UN Comtrade data are disaggregated to generate national and country-commodity level results, making it useful in identifying sectors where illicit flows are prevalent, but data are vulnerable to alteration or misstating by national customs agencies who report information. Comtrade data also doesn't distinguish between trade misinvoicing (unrelated parties) and transfer mispricing (related parties).

MONEY HELD OFFSHORE AND IN TAX HAVENS

Holding money offshore is big business – for corporations and criminals alike – but it's also a major factor when trying to understand the impact of illicit financial flows. These estimates look at the amount of money that is estimated to be held offshore, often unreported, around the globe. **In 2015, economist Gabriel Zucman estimated that the amount of money believed to be held offshore was**

$7.6 Trillion [3]

By his estimate:

80% of Offshore Wealth is Undeclared [3]

$190 Billion Estimated Tax Loss Due to Offshore Wealth [3]

Three years earlier, **James S. Henry** of the Tax Justice Network estimated that the total amount of offshore wealth could be as high as

$21-32 Trillion [4]

CONSTRAINTS OF METHOD

Zucman's estimates are based on financial deposits, relying on the difference between reported assets and liabilities, which could underestimate the problem. Henry assumes total non-declaration of assets that have been moved offshore illicitly, which could overestimate the extent.

CORPORATE TAX AVOIDANCE AND PROFIT SHIFTING

Multinational corporations are gaming the system to move money into low- or no-tax jurisdictions, thereby lowering the amount of taxes they pay, often skirting their fair share. As dollars move artificially to low- or no-tax jurisdictions, government revenue streams dwindle and there's less to go around to invest in the drivers of development, like roads, schools, and hospitals. Nowhere is the impact of this greater than in developing countries.

Each of the following estimates look at different aspects of profit shifting, and their effects on government revenue. While none claim to estimate the problem in its entirety, the evidence is clear that profit shifting is a serious problem for rich and poor countries alike.

By analyzing the route money traveled to developing countries, **the United Nations Conference on Trade and Development looked to see if taxable profits** were artificially lower when the money was routed through specific jurisdictions. UNCTAD estimates that the amount of money lost by developing countries to profit shifting is $100 Billion each year. [5]

*** CONSTRAINTS OF METHOD**

Because UNCTAD focused on one method of profit shifting, the study is not able to provide a holistic estimate for profit shifting globally. Furthermore, there is a severe limitation of data and information needed to fully investigate the problem.

Another estimate from the **International Monetary Fund** looked at whether tax policies in some countries could have a 'spillover' effect on the tax revenues of other countries. The study concluded:

- $200 Billion in revenue lost each year by developing countries

- $400 Billion in revenue lost each year by OECD countries. [6]

*** CONSTRAINTS OF METHOD**

This report compared actual corporate income tax levels with those that would be collected if the base was proportional to the gross operating surplus, an approximation of a form of source based taxation. Data limitations mean that this can only be done for a relatively small amount of sample countries. This report also did not examine profit shifting involving conduit countries.

But another study from Alex Cobham and Petr Janský used data on US multinationals to see if a disproportionate amount of their profits were ending up in jurisdictions where they had little real economic activity. The verdict?
A resounding yes. For the limited group of multinationals studied, the estimated loss in tax revenue was roughly $130 billion. US multinationals were only shifting 5-10% of their global profits in the 1990s; that figure has now risen to 25-30%. [7]

*** CONSTRAINTS OF METHOD**

This report used public data, aggregated on a national level and subject to a number of suppressions. Without company-level disaggregate data, it's difficult to provide more than topline estimates that show the potential extent of the problem. Additionally, the report only examined multinational corporations in the United States.

SUMMING IT ALL UP

Illicit financial flows are a multi-faceted phenomenon that is difficult to estimate. They don't fit neatly into one box, and can't always be quantified precisely, due to the inherent secrecy involved in their movement. There isn't even total consensus how to define illicit financial flows. But while estimates may differ, some things are certain.

1. **Illicit financial flows are a tremendous problem.**

2. **They are proliferated by a financial system which allows jurisdictions to offer secrecy for purchase.**

3. **Low-income countries often suffer disproportionately from illicit flows, even though they have the least capacity to deal with the effects.**

4. **As we pour over various estimates, the only way to conclusively answer the question of 'just how big are IFFs' is through making key financial data publicly available.**

FINANCIAL TRANSPARENCY COALITION

1. Dev Kar and Joseph Spanjers, "Illicit Financial Flows from Developing Countries: 2004-2013," Global Financial Integrity (December 2015).
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3. Gabriel Zucman, "The Hidden Wealth of Nations: The Scourge of Tax Havens," University of Chicago Press (September 2015).
4. James Henry, "The Price of Offshore Revisited," Tax Justice Network (July 2012).
5. United Nations Conference on Trade and Investment, "World Investment Report 2015: Reforming International Investment Governance" (2015).
6. Ernesto Crivelli, Ruud De Mooij and Michael Keen, "IMF Working Paper: Base Erosion, Profit Shifting and Developing Countries," International Monetary Fund (2015).
7. Alex Cobham and Petr Janský, "Measuring Misalignment: the Location of US Multinationals' Economic Activity Versus the Location of their Profits," International Centre for Tax and Development (November 10, 2015)