



CATCH THEM IF YOU CAN

A **BRIEFING PAPER** ON HOW FINANCIAL TRANSFERS
FROM **POOR** TO **RICH** IS THE RULE, NOT THE EXCEPTION

(...AND WHAT YOU CAN DO ABOUT IT)

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(...and what you can do about it)

This briefing paper is primarily focused on financial transfers – those transfers to and from developing countries in the wider context of radical inequalities and human underdevelopment. It is an ongoing story that concerns each and every one of us – not just politicians, business people and policymakers.

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The **Catch Them If You Can** project led by 80:20 explores the idea of 'radical inequality' in the context of finance for (under)development, highlighting a shared global order of institutions and mechanisms that are shaped by the better-off and imposed on the worse-off.

Open to community groups, teachers, students, financial sector workers and the business community, community co-op supporters and more, the project will illustrate the impact of this reality on human development and on the social investments 'foregone' as a result through interactive community workshops and participant-led activities.

<https://8020.ie/CatchThemIfYouCan>



80:20 Educating and Acting for a Better World, based in Bray, Ireland, is a non-governmental organisation that promotes popular education on human development and human rights.

For 80:20, education is fundamental to understanding the shape and nature of our unequal world, to interacting with that world as well as to imagining and shaping a different world.

In this context, education is a necessary, vital and intrinsic part of the overall agenda for international justice, human development and human rights – it is never an 'optional extra'.



80:20 Educating and Acting for a Better World is a member of the EU-wide initiative **Citizens for Financial Justice**.

Citizens for Financial Justice (CfFJ) is a diverse group of 37 European partners – from local grassroots groups to large international organisations – with a shared vision of informing and connecting citizens to act together to make the global finance system work better for everybody. CfFJ aims to support the implementation of the Sustainable Development Goals (SDGs) by mobilising EU citizens to support effective financing for development.

This briefing paper was produced with support from the CfFJ network.

<https://citizensforfinancialjustice.org>

THE 5:1 REALITY

IN ONE YEAR...

{ Total official aid flows **to** poorer countries amounted to }
US\$146 billion →

+

{ Total financial outflows **from** poorer countries amounted to }
← US\$770 billion

=

For every \$1 that was transferred
TO → poorer countries,
←←←← \$5 was transferred **OUT**

In contrast

ESTIMATED COST OF FINANCING KEY HUMAN DEVELOPMENT NEEDS

(in the 59 lowest-income countries)



Education at all levels

US\$259
billion



Health

US\$225
billion



Basic Social Protection
(children, maternity,
disability, pension)

US\$105 billion

Figure 1: The 5 to 1 Reality

TRANSFERS FROM THE POOR TO THE RICH IS THE RULE, NOT THE EXCEPTION

This briefing paper is primarily focused on financial transfers – transfers to and from developing countries in the wider context of radical inequalities and human underdevelopment. It is an ongoing story that concerns each and every one of us – not just politicians, business people and policymakers.

The 5 to 1 reality outlined for 2017 on page 3 highlights a shared world order of institutions and mechanisms that are, in effect shaped by the better-off and imposed on the worse-off without sufficient consideration of ethics or impact. It is a world order in which all of us participate consciously or unconsciously and it is an order that can and needs to be challenged. Ultimately, the debate is about human dignity (and indignity), human rights (and wrongs) and sustainability (and unsustainability).

Below we offer some summary baseline numbers on the current state of the 'financing for development' agenda:

- **US\$1,000 billion plus...and counting** – in the 5 years from 2014 to 2018, net legal financial outflows (after deducting inflows including official aid and foreign direct investments) from Developing Countries to Developed Countries amounted to a total of US\$1,005 billion. This reflects the pattern of the past twenty years, one that is expected to continue in the years immediately ahead
- **At least US\$2 trillion, but maybe as much as US\$8 trillion and still growing** – in the period 2005 to 2014, the estimated illegal financial transfers from Developing Countries could have been as high as US\$3.5 trillion but if extended onwards to 2017 could be as high as a staggering US\$8.7 trillion. At least 45% of these funds are estimated to be destined for international tax havens and the other 55% to Developed Countries. Being able to divide these transfers between 'legal' and 'illegal' is becoming more and more difficult and is a major concern to regulators internationally as well as nationally.
- **Nearly US\$1 in every US\$2 goes through tax havens** – 50% of funds invested in Developing Countries by large corporations are now being routed ('legally') from or through a tax haven – this is a deliberate strategy. Research suggests that hiding assets in tax havens may cost developing countries as much as US\$120-160 billion a year. One-third of these flows are being routed through tax havens under the jurisdiction of G8 countries
- **'Out of Africa...and the poorest pay** – in 2015 alone, the countries of Africa were net creditors to the rest of the world to the tune of US\$41.3 billion. Much more wealth was leaving the world's poorest continent (US\$203 billion) than is entering it (US\$162 billion).

WHAT THIS MEANS IN TERMS OF BASIC HUMAN DEVELOPMENT:

- Finances and the opportunity to use them to tackle some of the poor world's most pressing problems is 'lost' in the jigsaw puzzle that is the international financial system
- It leads to reduced public and private investment and expenditure in vital services and projects for many of the world's poorest countries and people
- It slows down or even reverses progress on world hunger and poverty amongst those least able to respond

- It means fewer jobs
- It translates into fewer hospitals, doctors, teachers and schools, safe water and sanitation, roads etc.
- It promotes and supports corruption, criminality, money laundering, tax evasion and the diverting of public 'common-wealth' to private pockets
- It damages democracy, public transparency and the rule of law
- It flies in the face of international programmes such as the Sustainable Development Goals (SDGs).

In short, it leads to the opposite of finance for development – finance for underdevelopment.

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WHAT REALLY IS A MILLION, OR A BILLION.... OR A TRILLION?

Visualising the scale of the figures in this briefing paper and around the issues it deals with is daunting and can be confusing. Moving up from millions to billions and then trillions can be a leap in imagination for the vast majority of us.

To assist us in understanding the scales involved, think about the following:

- 1 million seconds equal 11 days
- 1 billion seconds equal 32 years
- 1 trillion seconds equal 31,710 years

Navigating the leap from millions to billions and trillions can give us a sense of perspective in how vast these figures are, and, how vast the injustice is as detailed in this briefing paper.

A trillion dollars - how \$100 notes would stack up

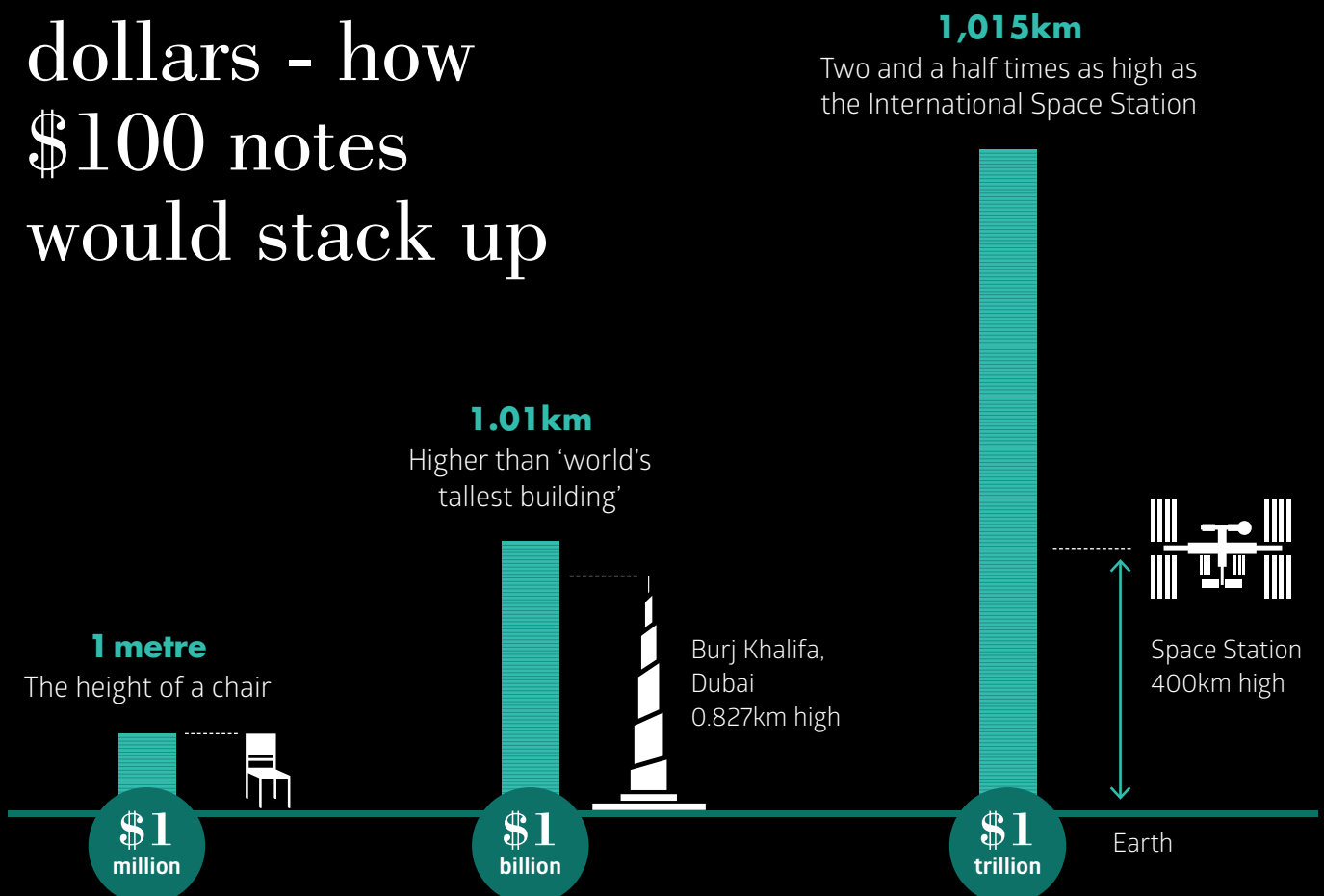


Figure 2: A trillion dollars - how \$100 notes would stack up

CONFUSED ABOUT LEGAL, ILLEGAL AND ILLICIT FLOWS? A NOTE ABOUT TERMINOLOGY

Illicit financial flows (IFFs) are illegal movements of money or capital from one country to another. According to advocacy and research NGO, Global Financial Integrity, this movement is classified as an illicit flow when funds are illegally earned, transferred, and/or utilised across an international border. Some examples of illicit financial flows might include:

- **A drug cartel using trade-based money laundering** techniques to mix legal money from the sale of used cars with illegal money from drug sales;
- **An importer using trade misinvoicing** to evade customs duties, value-added tax, or income taxes;
- **A corrupt public official using an anonymous shell company** to transfer dirty money to a bank account in the United States;
- **A human trafficker carrying a briefcase of cash** across the border and depositing it in a foreign bank; or
- **A member of a terrorist organisation wiring money** from one region to an operative in another.

GFI estimates that the annual value of trade-related IFFs in and out of developing countries has amounted to, on average, about 20 percent of the value of their total trade with advanced economies. There are three broad types of illicit activities:

1. **Breach of criminal laws**, such as money-laundering, and is usually termed evasion.
2. **Using often complex legal structures** to try to avoid the law (for those that can afford the services of expensive legal tax consultants). If such arrangements are discovered they may be challenged and found to be unlawful. Both of these can be termed illegal.
3. Some activities which are **against the public interest** manage to escape the legal net. Often laws are changed to prevent their future use.

Illicit financial inflows are also a serious issue. Common reasons for illicit inflows are tax evasion and for financing the illegal activities of international criminal networks engaged in human trafficking and smuggling of arms, drugs and valuable minerals. Both illicit outflows and inflows result in the same problem: taxes not being paid to governments.

Every dollar that leaves one country must end up in another. Very often, this means that illicit financial outflows from developing countries ultimately end up in banks in developed countries like the United States and United Kingdom, as well as in tax havens like Switzerland, British Virgin Islands, or Singapore. This does not happen by accident. Many countries and their institutions actively facilitate—and reap enormous profits from—the theft of massive amounts of money from developing countries.

How does 'illicit' differ from 'illegal'?

- Though many definitions of IFFs are limited to transactions that are *illegal*, determining whether a flow is *illicit* should go beyond assessing its legality.
- IFFs can include activities that are illegitimate, while not strictly illegal, as well as activities that go against established rules and norms.
- To determine if a flow is *illicit*, it is important to identify the relevant national legal framework(s), the degree of local enforcement and the ability of citizens to comply with the law.

Many international organisations and campaigning groups believe developed countries have a responsibility alongside developing countries to curtail the flow of illicit money.

Sources: *Illicit Financial Flows* by Global Financial Integrity; ENACT Africa; Tax Justice Network.

1. FINANCIAL TRANSFERS: WHO WINS, WHO LOSES?

Look at the figures and data on these two pages. What kind of stories do they tell, and how does that tally against headline messages about how much 'we' give?

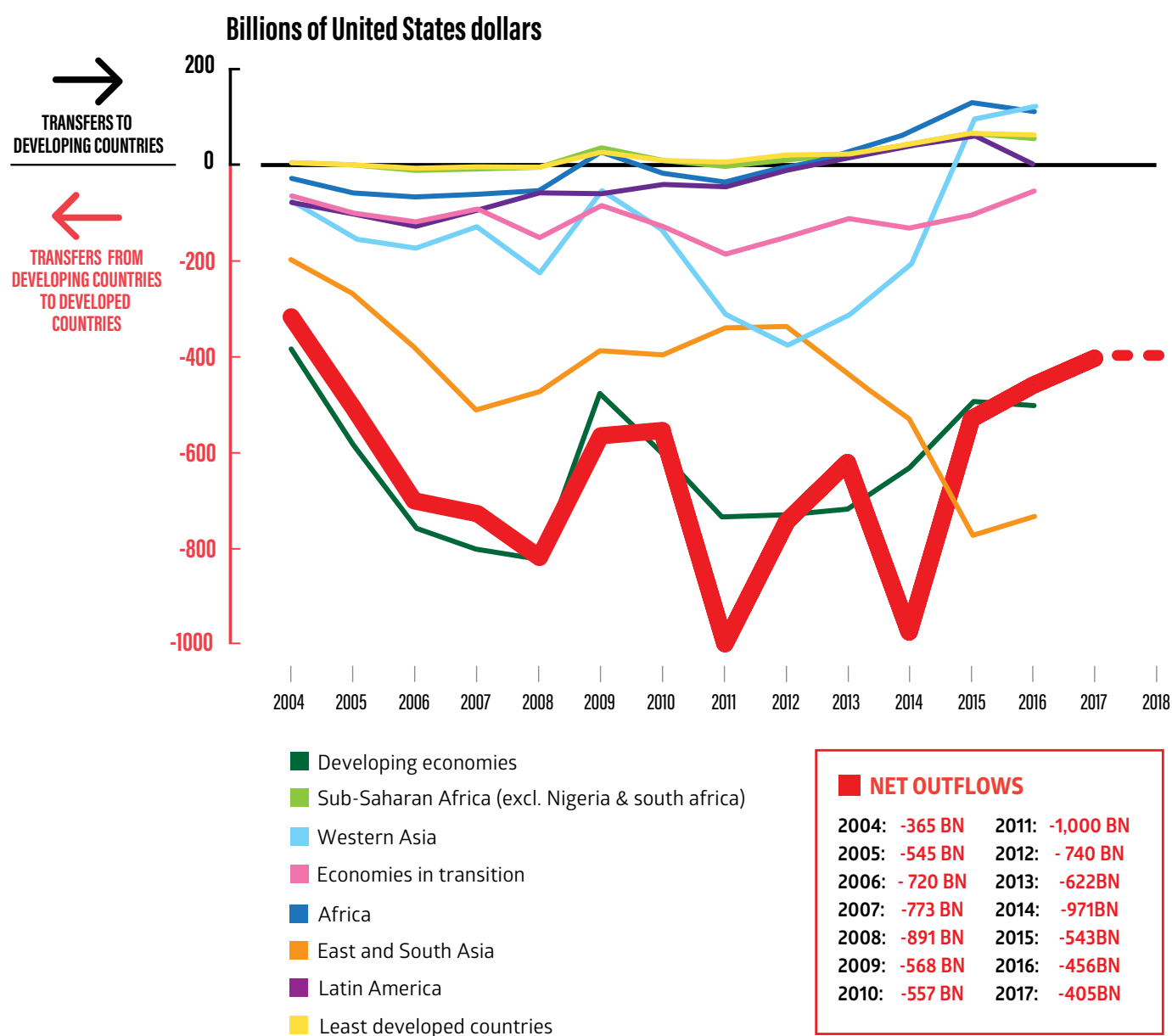


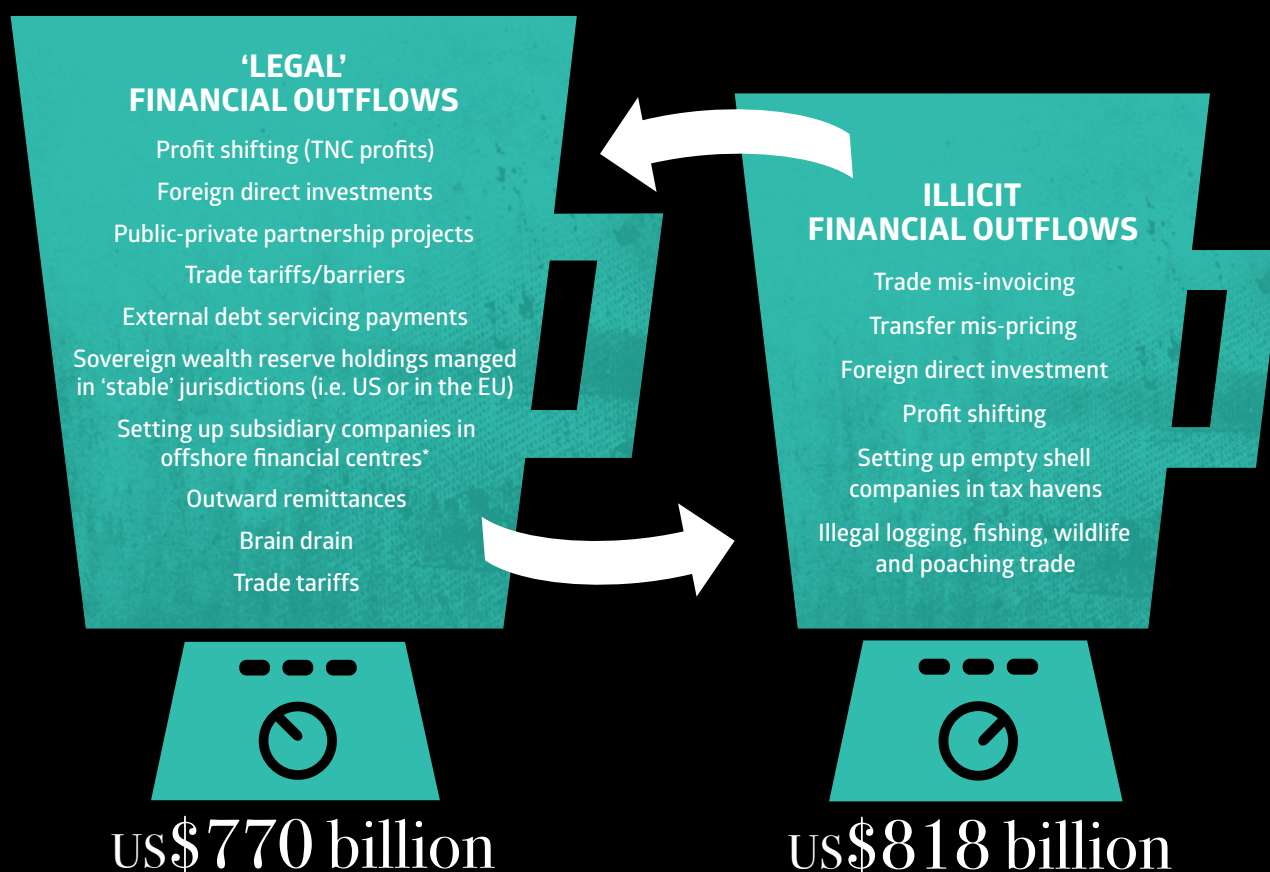
Figure 3: Net transfer of resources FROM developing economies and economies in transition TO developed economies between 2005 and 2017

Note: Net financial transfers are defined as net capital inflows (such as overseas aid, foreign direct investment) minus net interest and other investment income payments abroad (such as debt payments, storage of sovereign wealth reserves, profit sharing, trade tariffs etc.)

Source: World Economic Situation and Prospects Reports, 2005 - 2018; data: UN/DESA, based on data from IMF and World Bank;

Note: data has not been updated by UN DESA since 2018 and in the subsequent 2019 and 2020 WESP reports. Instead it is represented as a percentage of GDP.

Figure 4: Blending legal, illicit and illegal finance



US\$1,588 billion:
Minimum potential investments foregone

US\$400 billion

Annual financing gap required for all 59 of the world's lowest-income developing countries (LIDCs) to achieve the Sustainable Development Goals. (this calculation follows increases in domestic budget revenues, overseas aid and estimated philanthropy to 2030)

Sample costs to finance the SDGs across the world's 59 lowest income countries:



Education

US\$259 billion
(primary, secondary, tertiary)



Social Protection

US\$105 billion
(child and orphan benefits, maternity, disability, pension)



Biodiversity

US\$9 billion



Infrastructure

US\$208 billion
(energy, flood protection, irrigation, transport, water sanitation & hygiene, telecommunications)



Health

US\$225 billion

*Note: The Sustainable Development Solutions Network costed the financing gap to achieve the SDGs in its 2019 report, **SDG Costing & Financing for Low-Income Developing Countries** (LIDCs) based on IMF, OECD and World Bank data. For more, see <https://www.unsdsn.org>*

4 KEY ARGUMENTS.

US\$405 BILLION AND COUNTING...

According to the UN's annual report World Economic Situation and Prospects 2019:

'Net financial transfers to developing countries remained negative in 2017, albeit less so than in previous years, thanks to a recovery of capital inflows. In total, the net transfer of financial resources from developing and transition countries to developed economies is estimated at US\$405 billion, corresponding to 1.3 per cent of their aggregate GDP.'

Five years earlier in 2014, the UN acknowledged the scale, reality and impact of global financial transfers from poor to rich countries arguing that the resources extracted from poorer countries *'could be invested domestically to achieve greater economic, social and environmental outcomes'* (2014: 64).

In effect, these financial resources, urgently needed to fund basic human development in poorer countries, are being used to fund and support 'development' in richer countries and to make those already rich (in world terms) even richer.

This picture is simply not compatible with the long-term investment needed for ethical, sustainable or just development.

Current global financial flows impact on the poor in three key ways:

- The legal (and importantly also illegal) outflow of financial resources from Developing Countries undermines human development for the world's poor and threatens to negate much of the progress made in recent decades
- Such financial transfers contribute directly to increasing inequality worldwide with inevitable consequences economically, politically and environmentally

- They contribute to the undermining of democracy, accountability and transparency (through the routine and 'normal' use of secrecy and manufactured complexity) and through undermining the law

ARGUMENT 1:

Global financial transfer patterns over the past two decades directly undermine the achievement of internationally agreed targets for hunger and poverty eradication

The UK-based Overseas Development Institute has assessed the financing gap for three key human development agendas – health, education and social protection – as an estimated US\$2.4 trillion. Based on such estimates (and those of many other reports and commentators) funding from both state and private sources for these agendas are *'inadequate, volatile and not dependable'*. The financing gap for programmes such as the SDGs is very substantial with the majority of it needed in developing countries.

As noted by Christian Aid in the UK, this gap represents a challenge, but by no means an insurmountable one – *'far from it'*. Contrary to popular opinion, the resources already exist to deliver the Sustainable Development Goals and related agendas; they just need to be harnessed and managed differently. Sadly, this is not the case today – far too much of global wealth and finance is focused on re-enforcing the wealth of the already wealthy.

CASE STUDY 1

AFRICA IS NOT POOR...'

Central, Southern and West Africa, Western Asia, and Latin America and the Caribbean are home to some 275 million people living in extreme poverty. However, each of these regions continue to experience negligible levels of growth in per capita gross domestic product (GDP) and/or significant fluctuations in investment and basic expenditure in key areas of human development.

Planning for adequate investment in promoting basic human needs depends crucially on the availability and dependability of financial resources. Yet, as highlighted on page 1 (and, in more detail on pages 4-5) such resources continue to drain out of these regions at an alarming rate.

This inevitably means that agreed targets for eradicating poverty and creating decent jobs for all are pushed further and further into the future. As the UN World Economic Situation and Prospects Report for 2018 stresses:

'Failure to address these issues may leave a quarter of the population of Africa in extreme poverty by 2030.' (Sharples, Jones and Marples p.ix)

'Africa is not poor; but a combination of inequitable policies, huge disparities in power and criminal activities perpetrated and sustained by wealthy elites both inside and outside the continent are keeping its people in poverty.' Sharples, Jones and Martin

ARGUMENT 2:

The structure and operation of the global financial systems and the resource transfers it promotes and supports undermine other strategies to raise vital public resources (through normal taxation) and, as such, misuse local wealth and resources.

Global financial transfers are fuelled by the relentless 'logic' of increasingly globalised economies, financial structures and practices. As recognised by institutions such as the International Monetary Fund, the Organisation for Economic Cooperation and Development and the World Bank, local development (especially in Developing Countries) is highly dependent on international policies, frameworks, practices and agreements. It is now commonplace for these institutions to note that international monitoring, regulation and control is very weak. This reality facilitates the continuing use of transfer pricing practices, exploitative tax loopholes and opportunities; manipulative accountancy practices (especially by Transnational Corporations) and extensive use of tax havens.

Developing countries frequently raise a great proportion of their revenue from corporate tax and recent experience indicates that the sums involved in, for example tax avoidance are very significant in relation to overall revenue. Attempts to effectively regulate and control monetary transfers and practices is expensive financially and administratively, especially for developing countries

CASE STUDY 2

THE NEGATIVE CONTEXT OF INTERNATIONAL FINANCIAL TRANSFERS FOR THE ACHIEVEMENT OF THE SDGS WAS HIGHLIGHTED IN THE REPORT OF THE SECRETARY-GENERAL TO THE UN GENERAL ASSEMBLY IN JULY 2018:

...In aggregate, developing countries recorded capital outflows of US\$255 billion in 2017, following outflows of US\$431.5 billion in 2016. The lower level of capital outflows in 2017 largely reflects flows to China, which moved from a position of large net outflows in 2015 and 2016 to net inflows of US\$148 billion in 2017.

... Net portfolio flows to developing countries, which are driven primarily by institutional investors, remained volatile. They recovered from earlier outflows to reach US\$163 billion, driven by the recovery in flows to China. However, this was counterbalanced by net outflows of US\$136 billion in the “other investment” category, primarily cross-border bank loans. Regionally, emerging and developing Asia saw inflows in cross-border bank loans, although this is projected to reverse in 2018. Latin America and the Caribbean saw a nearly 2 per cent year-on-year decline in cross-border bank exposure in mid-2017, although this recovered in the second half of the year. (p3.)

...To achieve the Sustainable Development Goals, the global financial system will need to allocate long-term public and private resources for sustainable development in an effective and stable manner. Ultimately, stability and sustainability are mutually reinforcing: social, environmental and economic sustainability supports long-term stability, while without a stable financial system, achieving the Goals risks being derailed by future financial crises. (p2.)

ARGUMENT 3:

Current financial transfers and patterns contribute directly to increasing inequality worldwide

In its report on sustaining progress made during the era of the MDGs, the UN noted that the persistence of inequality at high levels in many developing economies has made it more difficult to reduce poverty. In circumstances of greater inequality, it is much less likely that economic growth can reduce poverty, regardless of the rate of that growth. The UN also notes that there is a growing consensus that extensive and systemic inequality can actually stunt growth itself.

Much of current research also indicates that international financial liberalisation has contributed to increased inequality. While some research

suggests that trade liberalisation improves overall welfare, the gains are small and very unequally distributed. For trade and investment to have the desired effect of reducing inequality and related poverty, a well-regulated, transparent and accountable international system of agreements is required.

And that is precisely what is currently missing in international trends and patterns. The result for the poorest countries and people is the current liberal trade and investment patterns sustain and even increase inequality.

CASE STUDY 3

AFRICA AND THE INTERNATIONAL ECONOMIC SYSTEM - WHO'S AIDING WHO?

'The reality is that Africa is being drained of resources by the rest of the world. It is losing far more each year than it is receiving. While US\$134 billion flows into the continent each year, predominantly in the form of loans, foreign investment and aid; US\$192 billion is taken out, mainly in profits made by foreign companies, tax dodging and the costs of adapting to climate change. The result is that Africa suffers a net loss of US\$58 billion a year. As such, the idea that we are aiding Africa is flawed; it is Africa that is aiding the rest of the world.'

This was one of the key conclusions of a 2014 research study *Honest Accounts? The true story of Africa's billion-dollar losses* published by 13 UK non-governmental organisations which explored the annual 'balance sheet' of financial resource flows in and out of Africa (excluding North Africa) in recent years. In noting that there were a number of outflows that they had been unable to calculate, the authors concluded that the figure of US\$192 billion was likely to be an underestimate; they also made no attempt to quantify historic costs and noted that not all inflows are automatically benefitting Africans or that all outflows are automatically negative.

In its 2017 update of *Honest Accounts*, the pattern remained: African countries receive US\$161.6 billion in resources such as loans, remittances and aid each year, but lose US\$203 billion through factors including tax avoidance, debt payments and resource extraction, creating an annual net financial deficit of over US\$40 billion.

The research shows that according to the most recent figures available (2015):

- African countries received around US\$19 billion in aid but over three times that much (US\$68 billion) was taken out in capital flight, mainly by multinational companies deliberately misreporting the value of their imports or exports to recuse tax.
- African governments received US\$32.8 billion in loans but paid US\$18 billion in debt interest and principal payments, with the overall level of debt rising rapidly.
- An estimated US\$29 billion a year was stolen from Africa in illegal logging, fishing and the trade in wildlife and plants.

ARGUMENT 4:

The current international financial system undermines democracy through ever-increasing secrecy and lack of accountability and through undermining the law

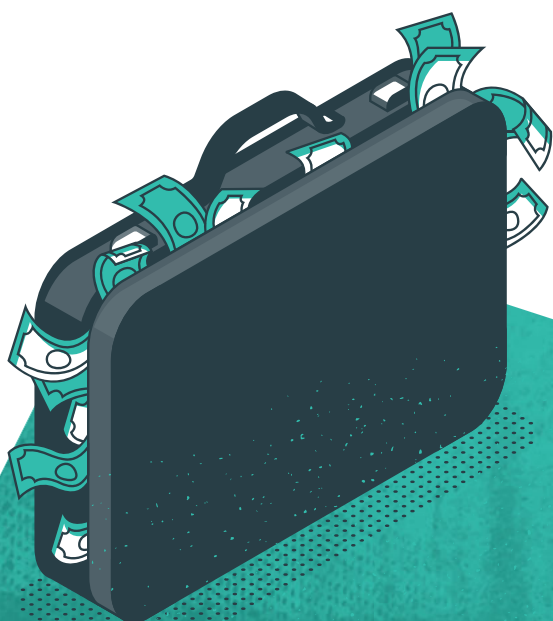
As business becomes more globalised, so too does its reporting, accountability and transparency. 'Modern' business has never been more complex with layer upon layer of 'real' and 'shelf' companies designed to maximise opacity and to avoid or reduce regulation and tax. It is now a reality that 50% of the wealth transferred through 'normal business behaviour' travels via a tax haven.

'The very existence of the global offshore industry and the tax free status of the enormous sums invested by their wealthy clients is predicated on secrecy : that is what this industry supplies as it competes for, conceals and manages private capital from all over the planet from any and all sources, no questions asked.'

J.S.Henry (2012) The Price of Offshore revisited, Tax Justice Network

In the Transnational Institute report State of Power 2019 Offshore Finance How Capital Rules the World researchers Reijer Hendrikse and Rodrigo Fernandez highlight how offshore finance is no longer an 'exotic sideshow' alongside regular and regulated finance, but has now become the new normal in much of business. While many Offshore Finance Centres are focused on providing secrecy and wealth protection to conceal illicit money, others now cater for corporations and banks seeking what is termed 'light touch' regulation in support of global financial flows. They argue that overall, global corporations have become predominantly focused around these offshore centres (especially since 2000) where, together with the world's billionaire class effectively they come to dominate not simply economics but also politics and the interpretation and implementation of law.

While wealthy countries' tax authorities struggle to chase money through these opaque places, their less well-resourced counterparts in developing countries have neither the resources, nor the economic or political muscle, to obtain the information they need about wealth squirrelled away in tax havens by companies and individuals.



2. GLOBAL FINANCIAL TRANSFERS – PATTERNS, TRENDS AND CONSEQUENCES

Such resource transfers consist of the net flow of funds to a country, including capital flows, capital servicing, income and current transfers (i.e. grants and other transfers, including official development aid), as well as the net change in a country's official international reserves.

- In the 5 years, **2014 to 2018, net capital outflows from Emerging Market and Developing Economies amounted to US\$1,005 billion** – projected to continue in 2019 and 2020 to an additional amount of US\$264 billion (IMF World Economic Outlook 2019: Table A13: 179)
- Overall, in 2017, **developing countries recorded capital outflows of US\$255 billion in 2017** (down on the figure of US\$431.5 billion recorded in 2016. This reduced level of capital outflows largely reflects increased flows to China (it changed from a position of large net outflows in 2015 and 2016 to net inflows of US\$148 billion in 2017)
- Estimates suggest that **hidden financial assets in tax havens alone may equal a loss to developing countries' public revenues of approximately US\$120-160 billion a year**. This is nearly three times the estimated cost of the agricultural investment needed to achieve a world free from hunger and twelve times the cost of ending the global of malnutrition
- Illegal tax evasion is not the only drain on the fragile public finances of developing countries. Billions of dollars are also lost through **legal tax avoidance by multinational companies and wealthy investors**, also enabled to a large extent by the world's tax arrangements
- **Debt continues to plague many of the weakest developing countries**, for low- and middle-income countries, the ratios of external debt to gross domestic product (GDP) have been rising since 2008. The International Monetary Fund (IMF) and the World Bank have reported that 18 low-income developing countries are at high risk of 'debt distress'
- **While African countries received around US\$19 billion in aid (in 2015), over three times that much (US\$68 billion) was taken out in capital flight**, mainly by multinational companies deliberately misreporting the value of their imports or exports to minimise or avoid tax.

'In 2017–2019, further setbacks or negligible growth in per capita gross domestic product (GDP) is anticipated in Central, Southern and West Africa, Western Asia, and Latin America and the Caribbean. These regions combined are home to 275 million people living in extreme poverty. This underscores the importance of addressing some of the longer-term structural issues that hold back more rapid progress towards sustainable development and to ensure that the targets of eradicating poverty and creating decent jobs for all are not pushed further from reach. Failure to address these issues may leave a quarter of the population of Africa in extreme poverty by 2030.'

- World Economic and Social Prospects 2018 report

3. WE ARE ALL INVOLVED, USUALLY UNKNOWNINGLY

In recent years an international network of investigative journalists uncovered a vast trove of over 13 million documents (named the Panama Papers in 2016 and the Paradise Papers in 2017), revealing the tax affairs of the corporate world and of wealthy individuals. The Papers exposed the deliberately complex structures that enable companies and individuals to avoid or minimise their taxes.

What was amazing about the papers was the scale of the 'secret' world of finance and the length that many go to 'manage' their wealth and to hide it from public scrutiny. Not just transnational companies but a huge array of individuals from musicians to actors, sportspeople to monarchs, business tycoons and professionals. The use of tax havens has become big business across the world with serious consequences for everyone.

What also became clear from the Papers is that we are all implicated although in most cases unknowingly.

With reference to tax havens and the layers of complexity surrounding them, multinational firms such as Facebook, Apple and Google constantly remind us that they are legal. The phalanx of lawyers and accountants that surround such companies insist that ethics do not enter the conversation as it simply 'business' with a view to maximising profit. The cost of this model to others or to human development is not part of their equation.

When we use Amazon, Google, Aviva insurance, Black & Decker, Citigroup, Facebook, Ikea, Pepsi, Skype, Starbucks, Vodafone or Walt Disney (or any one of another 350 transnational companies that make use of such tax reduction schemes) we become involved. One much publicised example is that Apple continues to use Ireland in order to minimise its tax liabilities (this is now the subject of EU legal procedures).

In November 2017, it was reported that several wealthy Irish entrepreneurs used such structures to buy private jets (and avoid VAT) by importing them through the Isle of Man. Musicians such as U2, actors in programmes such as Mrs. Brown's Boys etc. use similar schemes. While states such as Ireland become concerned at the loss of revenue, the impact of such international finance arrangements for poorer countries can be devastating.

Tax avoidance or 'minimisation' is not victimless. It results in funding losses for many basics – healthcare, schools, libraries, transport, roads and social welfare supports for the poorest. For example, a million lost in VAT on a single jet; a couple of million that would otherwise be owed on salary payments or royalties. The Tax Justice Network estimates that US\$21 to 32 trillion of private financial wealth is located in secrecy jurisdictions around the world.

The Network has developed a financial secrecy index to capture the nature and scale of the issue. It's 2018 Index challenges many popular ideas of the typical tax haven (e.g. Bermuda etc.). The top 10 such locations were Switzerland, the US, Caymen Islands, Hong Kong, Singapore, Luxembourg, Germany, Taiwan, the United Arab Emirates and Guernsey. Ireland is listed in 26th place on the Index (from 112 countries).

In the case of transnational companies, the figures are astronomical - in Apple's case offshore cash is worth more than US\$250 billion, more than the GDP of Portugal, New Zealand, Guatemala and Jordan.

AMAZON, ITUNES AND THE CAYMAN ISLANDS

Buying from Amazon often means that your purchases have been routed through a complicated structure hosted (but only on paper) by the Grand Duchy of Luxembourg, where Amazon's European headquarters are located. This is done to slash Amazon's tax bills around the world. In the past decade the company has been accused of consistently underpaying taxes due to deploying complex accountancy practices..

If you listen iTunes or use any of the many Apple products, you also become part of this global picture. The tech giant has been the focus of intense EU and US scrutiny for tax avoidance through setting up offshore corporations legally incorporated in Ireland and the US but for tax purposes, not resident anywhere. In 2016 the EU ruled that Apple's tax arrangement in Ireland was illegal and that it owed up to 13 billion euros (US\$14 billion) in back taxes. The Irish Government disagreed and were vindicated in July 2020 by the EU's General Court which found the 0.005% corporate tax rate that Apple had availed of in Ireland did not constitute illegal state aid. Other EU members, Luxembourg and the Netherlands, have appealed similar Brussels tax rulings against Starbucks Corp. and Fiat Chrysler Automobiles NV.

When Hurricane Ivan headed towards the Cayman Islands in 2004, it sent a stream of light aircraft racing to Miami. They contained computer hard disks, relating to a large slice of the world's Cayman-held wealth. (Banking assets in Cayman account for nearly a 15th of the world's US\$30tn in banking assets.) When the storm passed, they flew them all back again.

Source: Amazon made an US\$11.2bn profit in 2018 but paid no federal tax, The Guardian, February 15, 2019; European Commission, July 2020.



HOW IT WORKS 1 CORPORATIONS AND 'TRANSFER PRICING'

"Let's say a corporation picks and packs a container-load of bananas in Ecuador, and it costs the company US\$1,000. It sells them to a French supermarket for US\$3,000. Which country gets to tax the US\$2,000 profit – France, Ecuador? The answer is, "Where the multinational's accountants decide."

The multinational sets up three companies, all of which it owns: EcuadorCo, HavenCo (in a zero-tax haven) and FranceCo. EcuadorCo sells the container to HavenCo for US\$1,000, and HavenCo sells it on to FranceCo for US\$3,000. That's basically it. (The bananas themselves don't go anywhere near the tax haven: this is all just paper-shuffling in New York or London.)

If you blinked, you may have missed what happened here. It cost EcuadorCo US\$1,000 to pick and pack the container, and they sold it on for US\$1,000. So EcuadorCo records zero profits, meaning no taxes. Likewise, FranceCo buys it for US\$3,000 and sells it to the supermarket for US\$3,000. Again, no profits, and no taxes. HavenCo is the key to the puzzle. It bought the container for US\$1,000 and sold it for US\$3,000 – a US\$2,000 profit. But it is based in a haven, so it pays no tax. In short, all the profits have been stripped out of France and Ecuador, and shovelled into the haven. Hey presto!

In the real world, things are more complicated. Countries put in place defenses against this kind of nonsense, but the lawyers find ways to get around them, in a constant game of cat and mouse. These games transfer wealth from taxpayers towards corporate shareholders. This isn't about creating wealth, but about one group of people extracting wealth from another group. These transactions boost inequality, every time."

Source: Follow the money: inside the world's tax havens by Nicholas Shaxson, The Guardian, June 19, 2015



HOW IT WORKS 2

STATE AID AND TOOLS OF ATTRACTION

Tax expenditures may be defined as provisions of tax law, regulations, or practices that reduce or postpone revenue for certain taxpayers (such as transnational corporations) relative to a benchmark tax, such as corporate tax.

Governments are sometimes attracted to tax expenditures because they reduce revenue rather than the alternative of increasing spending (and so appear not to add to the size of government). On the other hand, tax expenditures can reduce the transparency, efficiency, and ownership of the financial system. Tax expenditures usually are given legal status by amendment to revenue laws. They can take several forms:

- **Allowances:** amounts deducted from the benchmark to arrive at the tax base;
- **Exemptions:** amounts excluded from the tax base;
- **Rate relief:** a reduced rate of tax applied to a defined class of taxpayer or taxable transactions;
- **Tax deferral:** a delay in the requirement to pay tax; and
- **Credits:** amounts deducted from the tax liability

While the underlying concept of the cost of tax expenditures is 'revenue foregone,' the methodologies for the measurement of tax expenditures are a matter of debate and discussion, especially regarding the definition of the tax base and measuring the expected behavioural responses of taxpayers in the absence of the tax expenditure.

Source: adapted from OECD, *Tax Expenditures in OECD Countries*, 2010; Healy, C. and M. Mansour, "Tax Expenditure Reporting and its Use in Fiscal Management: A Guide for Developing Countries". IMF, Fiscal Affairs Department, *How to Notes*, March 2019



HOW IT WORKS 3

HOW TO SHIFT PROFITS INTO A TAX HAVEN

World Inc. grows a crop in Africa, then harvests and processes it, transports and sells the finished product in the United States. It has three subsidiaries: Africa Inc. (in Africa), Haven Inc. (in a zero-tax haven) and USA Inc. (in the U.S.).



Africa Inc. sells the produce to Haven Inc. at an artificially low price. So Africa Inc. has artificially low profits – and therefore an artificially low tax bill in Africa.



Haven Inc. sells the product to USA Inc. at a very high price – almost as high as the final retail price at which USA Inc. sells the processed product.



USA Inc. also has artificially low profits, and an artificially low tax bill in the U.S. But Haven Inc. is different: it has bought cheaply and sold at a very high price, creating very high artificial profits.



Haven Inc. is located in a tax haven and pays no taxes on those profits.



Voila! A tax bill disappears.

Source: adapted from Tax Justice Network

4. ILLICIT OR ILLEGAL FINANCIAL TRANSFERS – A SUMMARY

Every year huge sums of money are transferred out of developing countries illegally with devastating consequences. Such illicit financial flows divert resources from developing countries – resources that could be used to finance much-needed public services, from basic social services such as health and education to agricultural and urban infrastructure investment.

Ultimately, such transfers weaken developing country financial systems as well as their economic potential. Admittedly, such transfers occur in all countries – and have similar damaging consequences everywhere – however, the social and economic impact on developing countries is acute given their smaller resource base and capacity.

In a context of both legal and illegal transfers, it is worth noting that very few of the least developed countries (LDCs) are expected to reach the much vaunted Sustainable Development Goal target for GDP growth of ‘at least 7 per cent’ in the near future.

Estimates of the scale of illicit transfers vary considerably and are the subject of much debate but there is general agreement that such financial flows now exceed both investment and aid flows in volume.

NGO Global Financial Integrity (which regularly monitors such transactions) estimates that the value of illicit transfers amounted to on average, over 20% of developing country trade with advanced economies in the 10 years between 2006 and 2015. In addition, it estimates that trade mis-invoicing is the primary mechanism for illicitly shifting funds between developing and advanced countries – accounting for upwards of 87% of such transactions that can be measured at present.

- An analysis of illicit financial flows related to trade alone for 135 developing countries in the period 2008 – 2017 indicates a value loss of US\$8.7 trillion; the figure for 2017 amounts to US\$817.6 billion.

- The developing countries with the largest average value gaps as a percent of total trade between the 135 developing countries and all trading partners in the same period include the Gambia – 47%, Seychelles – 38%, Paraguay – 27%, Ghana – 26% and the Bahamas – 26%.
- The average sizes of the value gaps in terms of dollars amount between developing world regions and the 36 advanced economies over the ten-year period were Asia – US\$476 billion, Developing Europe – US\$168 billion, Western Hemisphere – US\$131 billion, Middle East/ North Africa – US\$71 billion and Sub-Saharan Africa – US\$27 billion

One snapshot in 2014 reveals:

- US\$620 billion-970 billion drained from developing world in 2014, primarily through trade fraud
- Illicit inflows similarly harmful and estimated at US\$1.4 – US\$2.5 trillion in 2014
- Combined, illicit outflows and inflows accounted for 14% - 20% of total developing country trade in the years 2005-2014
- Sub-Saharan Africa continues to suffer most from such illicit outflows as a percentage of GDP

The most immediate impact of illicit financial flows (IFFs) is a reduction in domestic expenditure and investment, both public and private. This means fewer hospitals and schools, fewer police officers on the street, fewer roads and bridges.

It also means fewer jobs. Furthermore, many of the activities which generate the illicit funds are criminal; and while financial crimes like money laundering, corruption and tax evasion are damaging to all countries, the effects on developing countries are particularly corrosive. For example, corruption diverts public money from public use to private consumption. We know that in general private consumption has much lower positive multiplier effects than public spending on social services like health and education. Proceeds of corruption or criminal activities will generally

be spent on consumption of items such as luxury vehicles, or invested in real estate, art, or precious metals (World Bank, 2006). The social impact of a Euro spent on buying a yacht or importing champagne will be very different from that of a Euro spent on primary education.

On another front, money laundering is harmful to the financial sector: a functioning financial sector depends on a general reputation of integrity, which money laundering undermines. In this way, money laundering can impair long-term economic growth, harming the welfare of entire economies.

AREA OF ILLEGAL ACTIVITY	VALUE (EST.) \$US
Drug Trafficking	US\$344 billion per year 2016 estimate (UNEP, Interpol)
Human Trafficking	US\$157 billion per year 2016 estimate (UNEP, Interpol, ILO figures)
Illicit Wildlife Trade and Plants Poaching	US\$7 - 23 billion per year (World Wildlife Fund 2010 and OECD 2012)
Counterfeiting	US\$288 billion per year (UNEP & Interpol 2016 estimate)
Illicit Trade in Human Organs	US\$600 million and US\$1.2 billion per year (WHO 2009)
Illicit Trade in Small Arms and Weapons	US\$31.5 – 3 billion per year (UN Office for Disarmament Affairs 2015 and UNEP&Interpol 2016 estimate)
Illegal Extraction and Trade in Minerals/ Mining	US\$12 – 48 billion per year (UNEP&Interpol 2016 estimate)
Illicit Trade in Diamonds and Coloured Gemstones	Diamonds US\$860 million – \$1.4 billion: coloured gemstones around US\$400 million (Brilliant Earth 2013)
Illegal Trade and Dumping of Hazardous Waste	US\$10 – 12 billion per year (UNEP&Interpol 2016 estimate)
Illicit Oil Trade	Average yearly value 2003-2010: US\$10.8 billion (United Nations 2012)
Illicit Fish Trade	US\$11 – 23 billion per year (UNEP & Interpol 2016 estimate)
Illicit Timber Trade	US\$50.7 – 152 billion per year (UNEP & Interpol 2016 estimate)
Illicit Trade of Art and Cultural Property	US\$4 to US\$5 billion per year (Interpol 2014)
Illicit Gold Trade	US\$2.3 billion per year (conservative estimate) (Enough Project 2013)

Table 1: Balance sheet of illegal activities (based on most recent available data)

5. THINKING ABOUT WHAT NEXT?

For more than three decades, workers organisations, journalists, NGOs, politicians, students and consumers alike have led actions calling for reform of the rules that regulate and guide the practices of institutions and corporations, both nationally and internationally. The agenda has now also become a major focus for the UN, the OECD, the Africa Progress Panel and the EU alongside other international structures.

A set of core principles aimed at improving the quality and impact of financing in the context of international human development, human rights and the SDG agenda has been suggested by many. Such principles offer a basis for assessing (and then challenging) the entire international financial framework, as recently proposed by Christian Aid UK in its *Financing Injustice* report (2019) and in *Spotlight on Financial Justice* report (2019). These include:

- If financing for human and sustainable development is to have its intended impact, then the international community, at every level, must urgently address the bigger picture that for many decades now the dominant pattern of financial flows has been from and not to developing countries.
- There is little point in attempting to improve the targeting and impact of human development and human rights focused investments if the 'business as usual' model of such transfers continues to operate unhindered.
- Principles governing all aspects of investment activity must begin to realistically include human rights, social and environmental responsibilities and ethical governance concerns must cease to be optional and instead become mandatory.

As outlined by Christian Aid in the context of private investments, they must become a 'good investment':

'It must have impact that goes beyond 'do no harm' and adds value, enabling poor countries to tackle the root causes of poverty; build stronger, more resilient national economies; and ultimately capture a more equal share of global income and wealth. We believe that investment and the regimes that govern it should be judged – by donors, civil society and developing country governments – on the difference they are shown to make, in five separate but overlapping areas.'

Five separate and overlapping principle areas to improve the quality of finance include:

- **Do no harm.** An absolute minimum requirement that investments should respect human rights and the environment. This is the core foundation of good investment, but it is not enough to ensure that investment is good.
- **Develop resilient and diverse national economies.** Good investment results in progressively higher-value goods and services being produced within domestic economies, and increases tax revenues which can be used to fund essential public services.
- **Tackle inequalities.** Good investment helps to ensure that the benefits of economic development are fairly shared. It enables poor and marginalised women and men to participate in the economy on fair terms by creating decent work and addressing different kinds of inequality.

- **Build a low-carbon, environmentally sustainable economy.** Good investment supports structural changes to production and consumption patterns, so that economic development can happen in a way that is consistent with maintaining the environmental life-support systems on which we all depend.
- **Accountable governance of investment.** Good investment is subject to careful scrutiny to ensure that it does not undermine national development priorities. Investors can be held to account to ensure that when something goes wrong, people who are hurt can get justice.
- Net financial resources will, on balance continue to flow out of developing countries to the benefit of developed economies in the years immediately ahead. In such a context, robust international co-operation, regulation and adjustment is urgently required to address this reality. While organisations such as the World Bank highlight phrases such as ‘Maximising Finance for Development’, **we would highlight the need to ‘Minimise Finance for Underdevelopment’.**

Such an approach implies a strategy on three levels:

1. **Short and medium-term policies focused directly on the raising of living standards and promoting basic opportunities among the most vulnerable and at-risk communities** alongside longer-term policies that address the fundamentals of international frameworks and practices, especially those that produce and reproduce poverty, marginalisation and inequality.
2. Fundamental to achieving such objectives is the **realignment of the dominant global financial architecture and practices as required in the context of the 2030 Agenda for Sustainable Development and the Addis Ababa Action Agenda** (a 2015 international agenda for financing development agreed in Addis Ababa). The latter agenda emphasised that the priority for financing in the context of human development was to build a refocused ‘enabling environment’, something the current financial system spectacularly fails to do.
3. **The need to take part in and lead change now in our personal and professional lives – this is an option open to all of us** from **progressive tax reforms** to **new finance mechanisms** such as a financial transaction tax on transnational finance activities (a ‘Robin Hood Tax’), a climate damages or carbon tax (where ‘the polluter pays’) linking **national investments** and **procurement exercises to human rights action plans** (and reporting). There are many innovative and immediately accessible agendas for change locally, nationally and in cooperation with others.

In its agenda for 2030, the international system has recognised that fundamental reform of the financial system is necessary but it is not sufficient; additional areas for action include the fight against illicit financial flows, the growing use and promotion of tax havens, the reform of international investment agreements and continuing challenges with the burden of external debt.

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This briefing paper is primarily focused on financial transfers – those transfers to and from developing countries in the wider context of radical inequalities and human underdevelopment. It is an ongoing story that concerns each and every one of us – not just politicians, business people and policymakers.



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