Executive summary

It is axiomatic that illicit financial flows (IFFs) in general and tax related IFFs (TIFFs) in particular pose systemic risks for the financial and tax systems of countries by hampering the efforts to enhance domestic revenue/resource mobilisation (DRM) and fostering inequality, creating poverty, insecurity and financial challenges, and undermining public confidence and trust.

The resulting effects of IFFs/TIFFs impede, among others, implementation of the United Nations (UN) 2030 Agenda for sustainable development (UN 2030 Agenda), including the 17 sustainable Development Goals (SDGs) as well as the African Union (AU) Agenda 2063 of African countries (AU Agenda 2063). It is important, therefore, to stress that DRM is at the heart of the UN 2030 Agenda as well as the AU Agenda 2063. Hence, helping countries to mobilise more domestic resources through taxation is a growing area of development practice.

One of the core objectives and the most pressing issue of the Addis Tax Initiative (ATI) Declaration 2025 is enhancing DRM through fair, effective and efficient tax systems. ATI partner countries have committed to foster DRM and increase their resources to invest in programmes that support the achievements of ATI Declaration 2025. Commitment 3 of the ATI Declaration 2025 emphasised particularly that ATI member countries need to apply coherent and coordinated policies to foster DRM and combat TIFFs which are the most devastating barrier to the afore-mentioned development agendas and commitments toward DRM. Thus, TIFFs issues are of critical importance for ATI partner countries that are endeavouring to mobilise domestic revenues needed to achieve the UN 2030 Agenda and the AU Agenda 2063, among other initiatives.

Currently, there is neither a universally accepted definition of IFFs/TIFFs nor consensus on what should be included in the scope of IFFs/TIFFs and how the component parts should be determined. IFFs/TIFFs are multi-dimensional, comprising several different kinds of activities, including flows originating from illicit activities or transactions to transfer of funds that have a licit origin, and flows stemming from licit activity being used in an illicit way. As a result, the concepts of IFFs/TIFFs have been understood and addressed differently by different stakeholders. Some define IFFs/TIFFs strictly as financial flows that are illegal in the way that they are created, transferred, or utilised outside the country where they are obtained. This definition will not accommodate practices such as tax avoidance that are orchestrated within legal framework but against the intent or object and purpose of the law, meaning they are legal but illegitimate. Others define IFFs/TIFFs broadly as all financial flows that have a negative impact on an economy taking into account all direct and indirect effects in the context of the specific political economy of the society. This study adopts the broader definition of TIFFs since financial resources crossing borders that are illegally or illegitimately earned, transferred, used, or concealed abroad negatively affect the source state of such resources.

The actual volume of IFFs/TIFFs and that of their different components is extremely hard to measure, and estimates vary widely because it depends on the choice of the methodology used. Despite difficulties in quantifying IFFs/TIFFs, there is a range of estimations made by different studies and reports of regional and international organisations. The various estimates provide evidence that confirms that IFFs/TIFFs are devastating economic and development issues that call for an immediate need for drastic action.

There have been various initiatives and policy recommendations issued or proposed by different international and regional organisations on tax matters and money laundering issues which can be used in combating TIFFs. For instance, the developments over the past decade to improve tax transparency, enhance interagency cooperation in fighting tax evasion and tax avoidance, as well as capacity-building initiatives for tax administrations can all be utilised by countries to better tackle TIFFs. This study discusses some of these initiatives and policy recommendations.

It is encouraging to observe that ATI partner countries have taken various regulatory measures to combat TIFFs despite the difference in the scope of the measures and magnitude of their implementation in these countries.

This study presents the main practices of some of the ATI partners countries that have participated in this study, with the aim to enable ATI partner countries take lesson from each other in combatting TIFFs. The study covers various policy and regulatory frameworks of the countries in combatting TIFFs including:

- policies, strategies and legal frameworks on tax evasion, tax avoidance, transfer mis-pricing, and trade mis-invoicing in cross border context as well as on transparency and exchange of information (EOI) in tax matters;
- institutional set-ups to enforce the policy and legal framework, their level of implementation and interagency cooperation;
- international cooperation for transparency and EOI in tax matters; and
- challenges, successes, and next steps in combatting TIFFs.

Some of the main conclusions and suggestions included in this study report are as follows:

- Most ATI partner countries' policies and strategies to tackle TIFFs stem from existing tax laws and none of them specifically refer to IFFs/TIFFs as a threat for their DRM efforts under their DRM strategies, development plans or economic policies.
- ATI partner countries' initiatives on transfer pricing (TP), transparency and EOI as well as commitments for international cooperation are encouraging despite a range of differences that exist in the countries' domestic provisions and their level of enforcement. They still need to be improved.
- Implementation of TP issues and EOI options are challenging in terms of collecting information for TP and EOI purposes and in coordinating the working relationship among different units or institutions.
- The issue of trade mis-invoicing and its negative effects are not well considered.
- The level of interagency cooperation in combating TIFFs is also very low as compared to the cooperation framework in fighting against money laundering.
- There are human and technological capacity limitations in tackling TIFFs including understanding the prevalence of IFFs/TIFFs and their revenue impact.

Based on the practices, lessons learnt, successes and challenges shared by the ATI partner countries involved in this study, we recommend the following to all ATI partner countries:

- strong political commitment and leadership are needed;
- develop a robust policy and legal framework against TIFFs – holistic approach;
- set up or strengthen institutions responsible to tackle TIFFs;
- create an effective interagency cooperation/framework;
- increase working on human and infrastructural/technological capacity building; and
- enhance transparency, EOI and international cooperation on tax matters.

The actions that can be taken by development partners or donors to improve the effectiveness of tackling TIFFs include:

- encouraging countries to join the international tax transparency and EOI forums including the MAATM MC. The more jurisdictions join the initiative, the less room there is for cross-border IFFs/TIFFs;
- increasing the awareness and acceptance of the threat of TIFFs by the relevant government officials to gain their practical commitment and to foster interagency cooperation; and
- enhancing or continuing to support training and capacity-building initiatives.