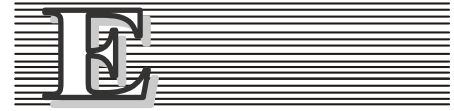




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**The State of Governance in Africa: The Dimension of Illicit Financial
Flows as a Governance Challenge**

List of acronyms

AU-ABC	AFRICAN UNION ADVISORY BOARD ON CORRUPTION
APRM	AFRICAN PEER REVIEW MECHANISM
ATAF	AFRICAN TAX ADMINISTRATIVE FORUM
IFF	ILLICIT FINANCIAL FLOWS
CFT	COMBATING THE FINANCING OF TERRORISM
FATF	FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING
IMF	INTERNATIONAL MONETARY FUND
MNCs	MULTINATIONAL CORPORATIONS
NEPAD	NEW ECONOMIC PARTNERSHIP FOR AFRICA'S DEVELOPMENT
OECD	ORGANISATION FOR ECONOMIC COOPERATION AND DEVELOPMENT
SEC	SECURITIES AND EXCHANGE COMMISSION
UNCAC	UNITED NATIONS CONVENTION AGAINST CORRUPTION
UNECA	UNITED NATION ECONOMIC COMMISSION FOR AFRICA
UNDOC	UNITED NATIONS OFFICE ON DRUGS AND CRIME
WTO	WORLD TRADE ORGANISATION

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I. INTRODUCTION AND BACKGROUND

1. Governing illicit financial flows has become one of main challenges confronting the surge for structural transformation in Africa. Illicit financial flows (IFF) perpetuate Africa's economic dependence on other regions and undermine the capacity of the African governments to articulate and implement a developmental state approach that prioritize capacity-expanding, transformative and distributive economic and social development policies. As outlined in the 2012 Economic Report for Africa (UNECA and AUC, 2012), unleashing Africa's productive capacity requires increasing investment in infrastructure, promoting technology transfer and innovation for value addition, and boosting agricultural productivity, among others. However, the quest for a developmental state in Africa has been significantly constrained by the financial structures of IFF, which undermine the potential for economic transformation in the continent through draining tax revenues and scarce foreign exchange resources, stifling growth and socio-economic development, and weakening governance.

2. African countries have been particularly vulnerable to the financial structures facilitating these illegal activities. Illicit financial flows out of Africa have become a matter of major concern due to the scale and negative impact of such flows on Africa's development and governance agenda. By some estimates, illicit flows from Africa could be as much as US\$50 billion per annum (Kar and Cartwright-Smith (2010)) and, indeed, the estimate may well be short of reality as accurate data does not exist for all transactions and for all African countries. Further, these estimates often exclude various forms of IFF such as proceeds from smuggling and mispricing of services.

3. The state's ability to pursue a developmental role depends to a large extent on its relative autonomy from the interest of powerful interest groups. In this context, illicit financial flows further deepen the unequal distribution of power (political and economic power) as the beneficiaries of IFF become wealthier and gain further control on the polity, which has adverse implications, notably on pro-poor policies. In other words, a major political cost of illicit financial flows is the undermining of the ability of African governments to implement developmental and transformative policies that run against the powerful interest groups that oppose these policies.

4. There has therefore been an increasing recognition of the state of governance as a major driver of IFF from Africa. The recent global financial crises have further highlighted the weaknesses in the regulatory mechanisms and the lack of transparency and supervision of cross border flows including the lack of regulation of onshore and offshore activities. Despite improvements in international laws and regulations against anti-money laundering processes, many African countries are still confronted with the difficulties of implementing practical measures to address this problem, given their underdeveloped financial markets and their limited capacity to enforce regulations.

5. High levels of corruption distort the allocation of public resources. In this context, resources are distributed in favour of those individuals that are willing and able to bribe and pay kick backs to public officials. Poor governance leads to public corruption and encourages corporate misbehaviour. The abuse of authority for private benefit is used by government officials and also typically by rent seekers in the private sector. Nevertheless, the relationship between the state of governance and the nature of illicit financial flows varies by country and is dependent on factors such as institutional weaknesses, historical propensities, economic structure and policies, and the state of the bureaucracy.

6. This parliamentary document examines illicit financial flows as a major governance problem in Africa. Section one highlights the main features of illicit financial flows and how the concept differs from capital flight. Section two focuses on the main estimates of IFF from Africa including the model developed by ECA. Section three examines the main development impacts of IFF while section 4 examines the broad issue of governance and the challenges confronting the various attempts to tackle illicit financial flows. Section five provides some conclusions.

II. ILLICIT FINANCIAL FLOWS: CONCEPTION, NATURE AND FEATURES

2.1 Definitional Issues: Transition from Capital Flight to Illicit Financial Flows

7. The subject of illicit financial flows is marred by a lack of terminological clarity, which somewhat limits the emergence of effective policy options. In many cases illicit financial flows and capital flight were used interchangeably.

8. Recent literature by the United Nations, Global Financial Integrity, the World Bank and others has defined IFF as money that is illegally earned, transferred, or utilized. Somewhere at its origin, movement, or use, the money broke laws and hence it is considered illicit (Reuter, 2012, Baker, 2005, Kar, 2011).

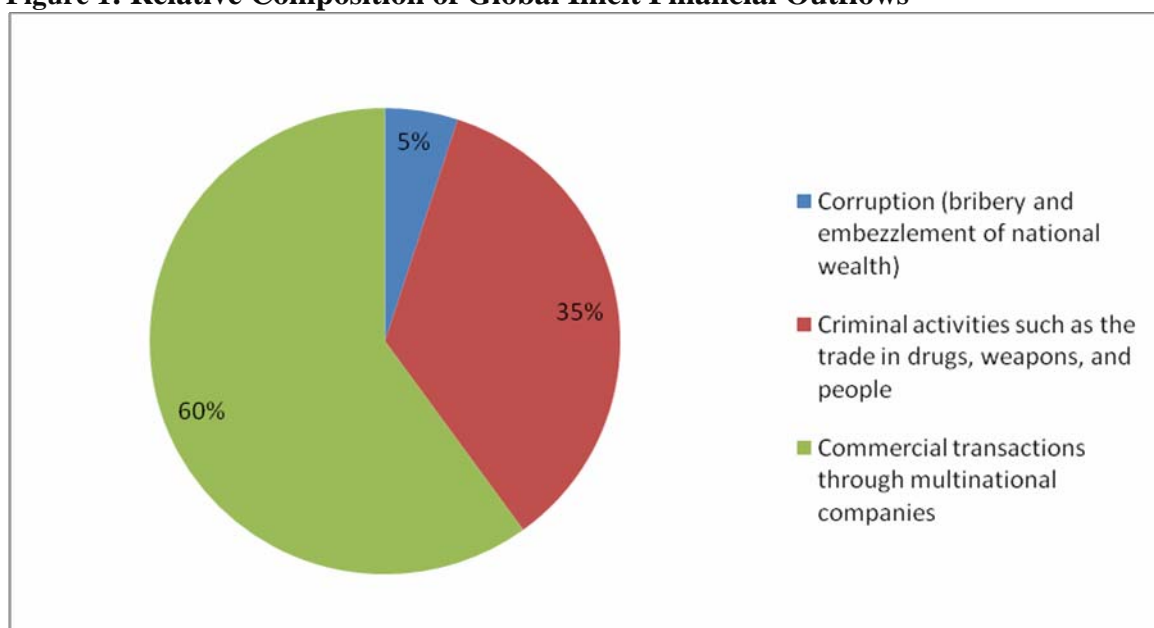
9. The definition above, which follows the pioneering work by Baker (2005), represents a major departure from the dominant notion of capital flight. Generally, capital flight is understood as the movement of funds abroad in order to secure better returns, often in response to an unfavourable business climate in the country of origin (Kant 2002, 354). Capital flight may be legal or illegal. However, illicit financial flows present a new conceptual conjecture that departs from capital flight both conceptually and in policy terms as shown below:

- The term illicit financial flows reflects a more narrow definition that focuses on unrecorded capital flows that derive from criminal, corrupt (bribery and theft by government officials) and commercial activities (Baker, 2005).
- The focus on hidden resources and their potential impact on development places the issue of capital flight firmly in the broader realm of international political economy which emphasizes the role of governance at both the origin as well as at the destinations. This stands in sharp contrast to the conventional models of capital flight, which tend to place the burden on developing countries rather than understanding the shared responsibility between developed and developing countries.
- The term illicit financial flows underpin a different manifestation of the state-market relationship to that characterizing the conventional work on capital flight. The latter approach, which is generally referred to as the portfolio choice (see Khan and Blankenburg, 2012) for more details) follows standard mainstream neo-classical models of utility and profit maximization whereas capital flight is explained as a portfolio diversification response by rational economic agents to higher foreign returns relative to domestic returns on assets. The emphasis on criminal, corrupt and commercial activities of IFF underlines a policy response that encourages a more active role for the State and that highlights the need for a better regulatory environment via enforcement of national and global standards of financial transparency and democratic accountability.

2.2 Main Components of Illicit Financial Flows

10. Illicit money can be classified into three main forms: (i) the proceeds of theft, bribery and other forms of corruption by government officials; (ii) the proceeds of criminal activities including drug trading, racketeering, counterfeiting, contraband, and terrorist financing; and (iii) the proceeds of tax evasion and laundered commercial transactions. Baker (2005) estimates that laundered commercial money through multinational companies constitutes the largest component of IFF, followed by proceeds from criminal activities, and lastly corruption (see figure 1.1). However, the proceeds of these components of IFF are so intricately connected that makes it virtually impossible to disentangle these components into concrete unified units. As discussed below, the cross-border nature of illicit financial flows highlights the critical need for a better cross-cutting analysis of IFF as a phenomenon.

Figure 1: Relative Composition of Global Illicit Financial Outflows



Baker (2005) quoted by Kar and Cartwright-smith, (2010).

11. According to the pioneering work by Baker (2005) and the subsequent Global Financial Integrity Studies (for example, Kar and Carthwright-Smith (2008), Kar and Curcio (2011)), corruption comprises 3-5 per cent of the total outflow of illicit funds. Corruption in this context is defined as the proceeds of theft, bribery and other forms of corruption by government officials. 12. It is highly likely that the figure above could be higher in Africa for a number of reasons. Firstly, the definition of corruption is rather narrowly defined as it focuses on bureaucratic or administrative corruption. In this context, corruption occurs when public officials misuse the trust place in them for private gain. This definition, somewhat underemphasize the involvement of private sector actors in illicit financial flows or the supply side of corruption, an important element of UNECA's program on policy, research and advocacy (see UNECA, 2012). Illicit financial flows are often the result of deliberate intentions and actions by private operators willing to evade regulation and oversight over their wealth, taking advantage of the opacity of the financial systems abroad.

12. The strict classification of the 'components' of illicit financial flows also takes a very narrow operational view of 'corruption' as a conduit of IFF. To the extent that these flows are illicit or illegal, they are in one way or another facilitated if not driven by corruption. Disentangling

corruption from other sources of funds such as tax evasion and criminal activities becomes therefore difficult at both the conceptual and empirical levels. For example, in the case of mis-invoicing, exporters and importers are able to manipulate invoices to channel money abroad or launder money by paying off regulators and inspectors. As highlighted by Chaikin and Sharman (2009:27) “corruption and money laundering are symbiotic: not only do they tend to co-occur, but more importantly the presence of one tends to create and reciprocally reinforce the incidence of the other”. Equally, corruption would facilitate transfer pricing. Multinational Corporations are able to buy off the relevant national authorities or even lobby in favour of low taxes, lax regulations and weak oversight provisions.

13. The above factors have made it difficult to accurately delineate the contribution of corruption to illicit financial flows and more substantially, this runs the risk of minimizing the problem of corruption as a facilitator of illicit financial flows. As a response to the challenges in tracking corruption and the lack of credible official data most empirical studies have relied primarily on how corruption is perceived. Perception of corruption is surveyed by several international and regional institutions including the World Bank’s ‘Worldwide Governance Indicators’, Transparency International’s Corruption Index, the Heritage Foundation’s Freedom from Corruption Indicator, and specifically for Africa, the UNECA’s African Governance Report and the Mo Ibrahim Index of Governance in Africa

14. The 2009 African Governance Report¹ (UNECA, 2009) highlights that corruption is a multifaceted phenomenon which poses a major challenge to governance and development on the continent and remains an issue even in countries characterized by higher levels of development. Particularly, the report notes that there is a strong presence of money laundering in the extractive industries. The report concludes that the major institutions of government (executive, legislature and judiciary) in Africa are prone to corruption to varying degrees. The private sector and non-state actors are also not immune to corruption. The report stresses that the performance of African countries in the area of budgetary oversight, for example, is somewhat weak due to a lack of resources and procedures in the auditor general’s office, deficiencies in the powers and exercise of oversight functions by parliament and lack of cooperation by the executive branch of the government.

15. Three key factors are considered to be correlated with lower levels of public corruption namely: strong institutions, a powerful anti-corruption constituency and better remuneration of public servants (UNECA, 2009). Botswana was cited by the Report as a prominent example of careful institutional reform that has promoted executive responsibility and accountability. Madagascar was also highlighted as a case that adopted some successful national anti-corruption strategies and put mechanisms in place to implement and monitor these strategies. The report asserts that despite the presence of these few positive cases, the general trend is that the national executive is engaged in corruption and arbitrarily makes use of public funds.

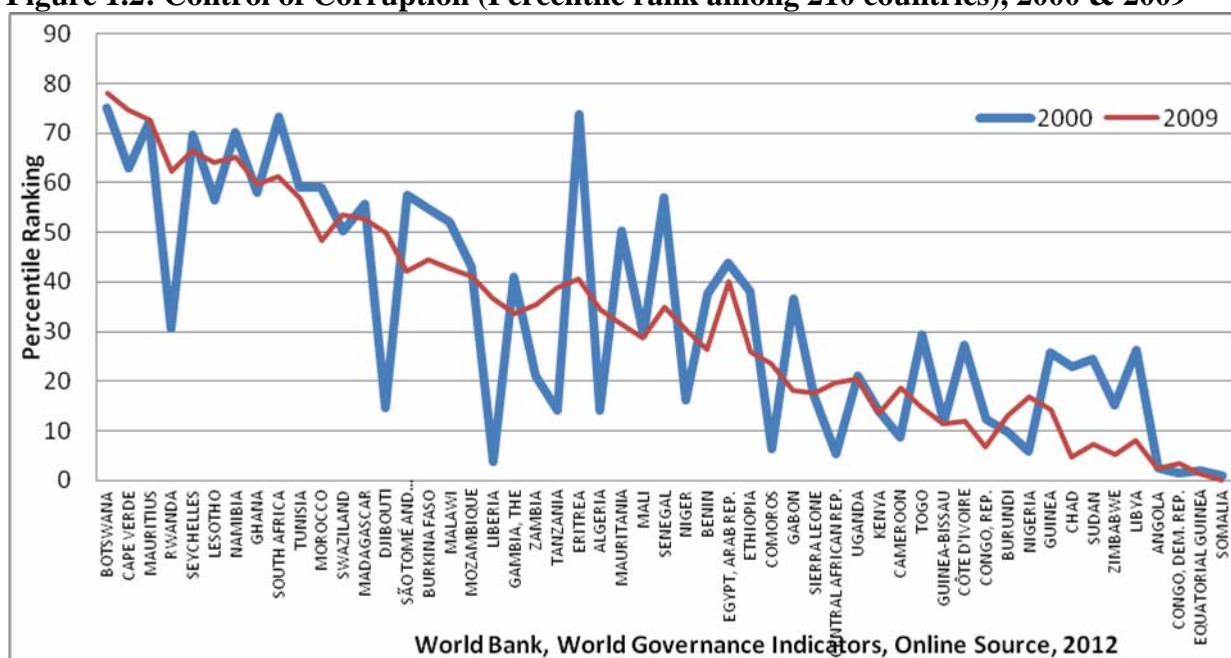
16. Botswana’s recent efforts on controlling corruption were also highlighted by the World Bank’s Worldwide Governance Indicators. The database focuses on six broad dimensions of governance for over 200 countries in the period 1996-2011. One of the broad dimensions is the ‘control of corruption’, with a percentile ranking between 0 (lowest control on corruption) to 100 (highest control on corruption) for 200 countries. For further details on the World Bank’s

¹ The AGR II report covers the following 35 countries: Benin, Botswana, Burkina Faso, Cameroon, Cape Verde, Chad, Republic of Congo, Djibouti, Egypt, Ethiopia, Gabon, Gambia, Ghana, Kenya, Lesotho, Madagascar, Malawi, Mali, Mauritius, Morocco, Mozambique, Namibia, Niger, Nigeria, Rwanda Senegal, Seychelles, South Africa, Swaziland, Tanzania, Togo, Tunisia Uganda and Zambia.

methodology, please refer to Kaufmann e.a., 2010. 210 countries/territories were surveyed (refer to Annex V for full details) to estimate the control of corruption in 2000 and 2009. One observation that can be drawn from the global level is that there was only one African country in the top 25 per cent percentile ranking (Botswana); another 10 African countries were above the top 50 per cent rankings, while 35 African countries were ranked below the 50 per cent percentile ranking out of the 210 countries. This implies that the perception towards the control of corruption in Africa is generally low.

17. The trend over the last decade shows that control of corruption varies across African countries (refer to Figure 1 below). Two observations are however worth mentioning. First, when comparing 2000 and 2009, there seems to be a general trend that African countries with high control on corruption in 2000 remained the same in 2009. Second, there are exceptions of countries which have significantly improved (thick line trend above the thin line trend) or significantly declined (thick line below the thin line) in the efforts to control of corruptions.

Figure 1.2: Control of Corruption (Percentile rank among 210 countries), 2000 & 2009



18. Recent figures by the 2011 Transparency International Corruption Perceptions Index² confirms the findings above and notes that the least corrupt country in Africa is Botswana which scored 6.1 and the most corrupt country is Somalia at 1.0. The ranking of other African countries varies significantly (Transparency International, 2011).

19. The remarkable rise in smuggling and human, drug and firearms trafficking over the past few decades highlights the difficulties of reaching a consensus on how to combat 'organized crime', a matter which has not been well researched. A prominent feature of this phenomenon is its close interlinkages with the other two sources of IFF namely corruption and commercial transactions through multinational corporations. Transnational organized crime permeates various segments of

² The Transparency International Corruption Perceptions Index ranks countries and territories according to their perceived levels of public sector corruption on a scale of 0 (highly corrupt) to 10 (very clean).

state and society by infiltrating government agencies and institutions as well as business and politics. Furthermore, it severely undermines governance and democracy as it empowers those who operate outside the law.

20. UNODC (2011) estimates that about US\$1.6 trillion (equivalent to about 2.7 percent of global GDP) was available for money-laundering activities across the globe. The largest income for trans-national organized crime seems to come from illicit drugs, accounting for a fifth of all crime proceeds. It is estimated that the illicit flow of goods, guns, people and natural resources is approximately \$650 billion. Illicit drug trafficking and counterfeiting are the two largest components of these criminal activities. The market for illicit drug trade is estimated to be worth \$320 billion (50 per cent of total) whereas the market for counterfeiting comprises \$250 billion (39 per cent) of total. Other sources such as human trafficking and illicit oil trade comprise respectively 5 per cent and 2 per cent of the total (Haken, 2011).

21. The UNODC World Drug Report 2012 estimates that drug trafficking generates between 20-25 per cent of all income derived from organized crime and approximately half of the income from transnational organized crime. The trend in illicit drug market seems to be stable and changes in flows can mainly be observed below the surface. This indicates that the illicit drug market is resilient and illicit drug suppliers and users are quick to adapt to preventative measures (UNODC, 2012).

22. Tracking the flows of illicit funds generated by drug trafficking and organized crime and analyzing the magnitude and the extent to which these are laundered through the world's financial systems remain daunting. A UNODC study on Transnational Trafficking in West Africa noted that much of the best information on contraband flows through the region comes from data sources outside the region. Still, the information remains sketchy and incomplete, and its interpretation is, in the end, a matter of judgment (UNODC, 2009).

23. Criminal activities and its relation to illicit financial flows has become a pressing concern in Africa the continent. Growth in international commerce and transport in conjunction with weak enforcement capacity and underpaid officials has made African countries an ideal conduit through which to extracting and transshipping illicit commodities. The West African states, in particular, remain subject to a set of structural vulnerabilities that render them exposed to the development of organized crime. The lack of capacity by police officers, investigators and prosecutors is further compounded by the governance response to the problem which essentially focuses on the individual criminals rather than the fluid structures of the criminal groups. A recent study suggests that, in the year 2011 alone, thirty tons of cocaine and around 400kg of heroin were trafficked in West Africa and it was estimated that criminal networks engaged in this trafficking generate annually \$900 million. Furthermore, the drug trafficking has created spill over effects in the region. West Africa has become a final destination for drugs and cocaine as heroine use has increased significantly. There are now some 2.3 million cocaine users in West and Central Africa. Moreover, increased production, trafficking and consumption of drugs in conjunction with piracy and insecurities makes West Africa a high risk region (UNODC, 2012).

24. Another integral area of transnational organized crime in Africa is the illicit smuggling of oil from Nigeria which is considered one of the biggest threats to the rule of law in West Africa. Its increasing magnitude and significance highlight reveal the major adverse consequences on governance and development in one of the largest countries in Africa and the possible negative externalities to the neighbouring countries.

25. Trade mispricing is a popular way of transferring illicit capital. The change in the magnitude of this type of IFF is directly related to the change in volume of trade during the period (1970 – 2008). Kar and Curcio (2011) showed that annual growth of IFF from developing countries in 2000 was 18 per cent while in 2007/8 it dropped to 12.9 per cent. However, this figure is expected to rebound as the world economy strengthens and as trade volumes rebound. As well, the associated decline in the share of trade mispricing in the last few years is expected to resume its contribution.

26. The most significant perpetrators of trade mispricing are multinational corporations (MNCs). This is due to their strong global presence and influence, which facilitate the illicit transfer of funds. The WTO estimates that MNCs control about 60 per cent of world trade, which amounts to about US\$ 40 trillion. Other forms of illicit commercial activities include tax evasion. These activities basically shift money beyond the reach and appropriate use of domestic authorities.

27. Wang (2008) provides an interesting assessment of illicit outflows from China through commercial activities. He suggests strong links between trade mis-invoicing, transfer pricing, tax-dodging, and reducing interest rate costs. In the case of China, firms will sell their goods at inflated prices to subsidiaries located in tax havens as a means to inflate production costs, thereby minimizing profits and ultimately their taxes. Wang further notes that given the deductibility of interest rate costs from their taxable incomes, firms can over borrow at low costs and subsequently transfer assets overseas to meet “debt service obligations.” What this effectively suggests is that firms utilize a variety of instruments comprising parallel loans, currency swaps, and quasi-money loans between subsidiaries and their joint venture partners to maximize their profits. Paradoxically, despite the compellingly high levels of illicit flows from China (the country lost 10.2 per cent of GDP or US\$ 109 billion in 1999 alone), it has maintained strong capital formation. (Murphy e.a., 2007) suggests that this is due to the fact that China offers investors lower tax rates, favourable land use rights, convenient administrative support, and propitious financial services, which collectively act as incentives for re-investment. Accordingly, it is estimated that as much as a quarter of the more than US\$100 billion of China’s illicit outflows return each year in the form of “round-tripping FDI.”

28. In addition to illicit financial flows, the focus of this paper, the lack of transparency and capacity also aid aggressive tax planning. Although it may not be strictly illegal, tax planning is not only immoral but also has detrimental effects on African countries due to their relative institutional weaknesses and their disadvantaged position vis-à-vis global corporations.

III. QUANTIFYING ILLICIT FINANCIAL FLOWS FROM AFRICA

3.1 Illicit Financial Flow Estimates for Africa

29. Accurate measurement of illicit financial flows has proven difficult due to the secretive nature of these transactions and owing to data limitations. However, a number of empirical methods have attempted to overcome these challenges to provide estimates of both the magnitude and the development implications of these flows for developing countries in general and African countries in particular. These empirical models and their underpinning analysis deserve further scrutiny. All these models conclude that Africa has been a net creditor to the rest of the world due to the considerable illicit financial outflows from the continent. It is, however, important to note that these estimates are conservative given inadequate data and the multifarious channels through which illicit capital flows occur.

30. Recent estimates of illicit financial flows differ in terms of assumptions and data sources but they all indicate considerable IFF from Africa. According to the most aggressive scenario (Kar and Carthwright-Smith (2010)), Africa lost about US\$ 854 billion in illicit financial flows over the 39 year period (1970-2008); corresponding to a yearly average of about US\$ 22 billion. The trend has been increasing over time and especially in the last decade, with an annual average illicit financial flow of US\$ 50 billion between 2000 and 2008 against a yearly average of only US\$ 9 billion for the period 1970-1999 (Kar and Carthwright-Smith (2010)). The decline in 2009, as registered in Kar and Freitas (2011), is likely explained by the recent economic and financial crises, which have depressed overall global trade.

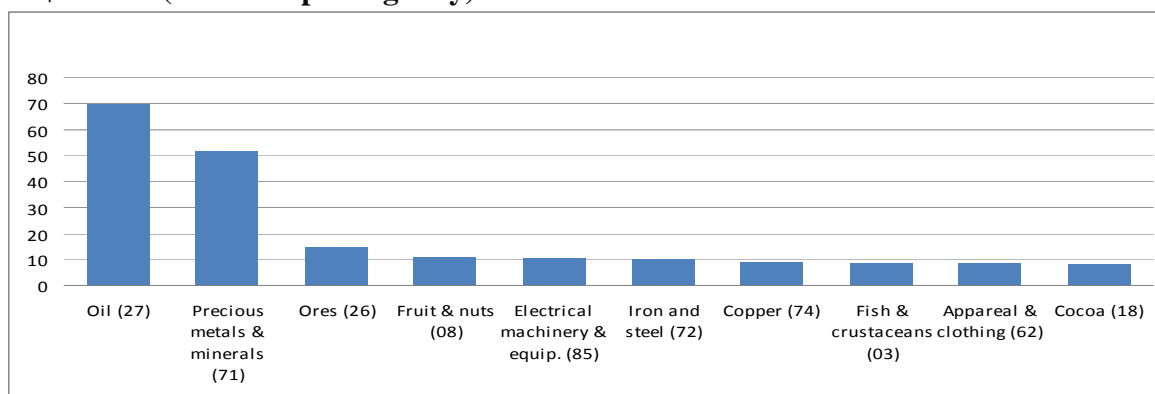
3.2 UNECA's Trade Mispricing Model: a Sectoral Analysis

31. The ECA has provided an empirical analysis of the trade mispricing component of illicit financial flows in Africa by sector, an area which has not yet been well examined in the literature.

32. The methodology adopted in this model compares bilateral data for the same trade flow, comparing country *i*'s exports of product *a* to country *j* with country *j*'s imports of product *a* from country *i*. Interestingly, this two-way information is usually mis-matched for several reasons: (i) exports are generally expressed free-on-board (FOB), while imports are normally reported including the cost of insurance and freight (CIF); (ii) the same product may not necessarily be classified using the same nomenclature by each country; (iii) mistakes in reporting the value of the flows are possible; (iv) delays often occur in the export/import process; and (v) illicit financial flows can also be considered as a source of discrepancies.

33. Illicit financial flows from Africa measured through trade mis-pricing show high concentration in a few sectors, notably the extractive and mining industries. Over the period 2000-2009, more than half (56 per cent) of the IFF from the African continent over the 10 years period arose from oil, precious metals and minerals, ores, iron and steel, and copper.

Figure 2.2: Top 10 Sectors (HS2 classification) by Cumulative IFF (2000-2009) for Africa – US\$ billion (trade mispricing only)



Source: UNECA's computations

34. Sectors such as edible fruit and nuts, electrical machinery and equipment, fish and crustaceans, apparel, and cocoa have also been targets for IFF over the period 2000-2009; each accounting for between 3 per cent and 4 per cent of total IFF from Africa over the past decade. The sectoral analysis also reveals a high IFF concentration by country for both extractive industries and other sectors such as edible fruit and nuts, electrical machinery and equipment, fish and crustaceans, apparel, and cocoa.

35. Concentration is also high in the destination countries. For example, 76.4 per cent of IFF in oil from Nigeria in 2008³ benefited only 5 countries, namely the United States, Spain, France, Japan and Germany. More generally, it appears that the main recipients of IFF from African countries are primarily developed countries (especially, the United States, Europe, Canada, Japan and Korea) and emerging economies (such as China and India). Interestingly, these countries are also Africa's major trade partners.

IV. DEVELOPMENTAL CHALLENGES AND CONSEQUENCES OF IFF FROM AFRICA

36. Africa forfeits significant volumes of financial resources, which could have been used to finance critical development projects, due to illicit outflows. This disturbing phenomenon has damaging effects on African countries, including: (i) draining resources and tax revenues; (ii) stifling growth and socio-economic development and (iii) weakening governance. These evidence are a glaring indicator of the adverse impact that illicit financial flows have on the continent's medium and long-term prospects for development.

4.1 Draining Resources and Tax Revenues

37. A major negative impact of illicit financial flows is the foregone government revenues through the erosion of the tax base. Decreased government revenue further depresses investment and may lead to higher levels of inflation tax, while depreciating the value of domestic assets.

38. Weak structural systems also expose African countries to the risk of falsified invoicing and transfer mispricing due to loose administrative constraints and limited resources to support investigation of tax evasion. According to one tax expert, to date no African country has managed to successfully conclude an investigation into transfer mispricing (Murphy, Christensen and Kapoor, 2007; Christensen, 2009).

4.2 Impact on Growth and Development

39. Due to the huge amount of IFF out of Africa, the continent has experienced lower levels of investment than other developing regions and this has hampered poverty alleviation programs and economic transformation efforts. For instance, some estimates show that if Africa were to repatriate illicit funds, the capital stock would expand by more than 66 per cent. Ancillary to this fact is that if the illicit outflow of funds did not take place, GDP per capita would have been 16 per cent higher than what it is in the current environment (Ndikumana and Boyce, 2008, 2011).

40. Despite the growth in GDP, average gross capital formation (as a percentage of GDP) in Africa was 19 per cent in the period 2000-2010. This figure is limited by the average gross capital formation in a country such as China which recorded an average of 42 per cent over the same period. Similarly, average domestic savings (as a percentage of GDP) in Sub-Saharan Africa was 16 per cent in the period 2000-2010. In the same period, members of the OECD recorded average domestic savings of 19 per cent and in China this figure came to 47 per cent (World Development Indicators, 2012).

³2008 being the year over the period 2000-2009 when IFFs were the highest for Africa.

41. Illicit financial flows also affect income distribution as citizens face higher taxes and austerity measures designed to finance external debt obligations. Higher tax burdens disproportionately fall on the poorer citizens and impinge on the ability of the State to provide social services (Ajayi 1997). Added to this, illicit flows can contribute to reduced investment, slower economic growth rates and high unemployment.

42. A large gap still separates Africa from its MDGs. By all accounts, official donor aid commitments will probably fall well short of the required funding of MDGs leaving open the serious possibility that related targets will recede even further. Hence, if the problem of illicit flows is not addressed as a matter of high priority, the poor will likely experience a further decline in access to basic services in the face of grinding poverty.

4.3 Weakening Governance

43. Financially weak States cannot operate effectively and are generally constrained from providing public goods and services/. IFF is also damaging to the State in as much as it undermines (through bribery and public theft) the various institutions (banks, financial intelligence units, legal systems etc) that are responsible for detecting and prosecuting IFF. It also discredits democratic institutions, which could be used to dispose of the proceeds of corruption, thereby fuelling further corruption.

44. High costs, distortion effects as well as resource drainage hamper economic performance. This is facilitated through tax evasion and other forms of IFF and the shift of resources from productive activities to speculative (unproductive) activities. In the latter case, investment is captured by commercial activities providing quick returns rather than by activities generating investment returns in the long-term such as manufacturing and agriculture sectors.

45. The allocation of public resources tends to be guided by the advancement of personal and group interests over national interests. In this regard, resource distribution is determined by rent seeking rather than productivity maximisation. Besides this, effort and time is devoted by the private sector to secure business licences or preferential access to markets instead of focusing on increasing productivity (Murphy, Shleifer and Vishny (1991) in UNECA, 2012).

46. Furthermore, illicit financial flows and corruption undermine the private sector by repressing entrepreneurship. Illicit financial flows and corruption negatively affect private sector development as businesses and entrepreneurship are suffocated; and structural transformation and economic diversification are significantly curtailed

4.4 Impact on Economic Dependence and the Challenge of Structural Transformation

47. IFF perpetuates Africa's economic dependence on other regions. Recent evidence highlighted in section 2 of this report show that Africa lost about US\$ 854 billion in illicit financial flows over the 39 year period (1970-2008); corresponding to a yearly average of about US\$ 22 billion. This cumulative amount is considerably high compared to both the external debt of the continent and the official development aid (ODA) received over the same period. Indeed, it is equivalent to nearly all the ODA received by Africa during that timeframe⁴ (see OECD (2012)).

⁴ US\$1.07 trillion of ODA was received by Africa between 1970 and 2008; computation based on table 2.2.9. of Chapter II of the OECD 2012 report on "Development Aid at a Glance – Statistics by region".

Also, only one-third of the loss associated with IFF would have been enough to fully cover the continent's external debt that reached US\$ 279 billion in 2008 (UNECA, Economic Report on Africa (2009))

48. IFF through its various channels negatively affect the opportunities for structural transformation in Africa. As outlined in the 2012 Economic Report for Africa (UNECA and AUC, 2012), unleashing Africa's productive capacity requires increasing investment in infrastructure, promoting technology transfer and innovation for value addition, and boosting agricultural productivity, among others. These activities require significant resources (estimated at over US\$ 90 billion per annum for infrastructure investment alone). Thus, resource savings from curbing IFF could help spur domestic resource mobilization, which is critical for financing the much needed investment in infrastructure for the continent's structural transformation.

V. CURTAILING ILLICIT FINANCIAL FLOWS: AN AFRICAN PROBLEM WITH A GLOBAL SOLUTION

49. Illicit financial flows pose a threat to the stability and security of African countries and undermine the institutions and democracy as well as jeopardize sustainable development and the rule of law. The inherent nature of illicit financial flows requires international cooperation and intervention. Illicit financial flows and corruption are a transnational phenomenon which makes international co-operation essential (UNCAC, 2003). This section examines the main challenges confronting this phenomenon and discusses the emerging African response to address the issue of illicit financial flows from the Continent.

5.1 The Political Economy of Illicit Financial Flows

50. Section three of this parliamentary document highlighted that illicit financial flows play a significant role in undermining the potential for economic transformation in the continent through draining tax revenues and scarce foreign exchange resources, stifling growth and socio-economic development, and weakening governance. This section takes the analysis further to examine the political economy impact of IFF. Illicit financial flows further deepen the unequal distribution of power (political and economic power) as the beneficiaries of IFF become wealthier and gain further control on the polity, which has adverse implications, notably on pro-poor policies. In other words, a major political cost of illicit financial flows is the undermining of the ability of governments to implement economic policies that run against the powerful interest groups that oppose these policies. Epstein (2006) underscores that financial 'globalization' has provided a conducive environment for a 'capital strike' against undesired taxation or regulatory policies. This has wider implications on the nature and the modes of development in African and the orientation of the domestic capitalists. Illicit financial flows create a vulnerable political environment and a vicious circle of weak and illegitimate domestic capitalism, where the business decisions are essentially influenced by foreign components as they see little incentive in nurturing the domestic institutions that would protect and encourage private investment (Moore, 2012).

51. Illicit financial flows reflect a high degree of articulation of international and domestic factors in an increasingly deregulated global economy. The incentives facing economic and political elites have been shaped particularly by the major changes in the global economy that took place since the late 1970s. The deregulated global financial markets have been an integral feature of the ideological shift towards neo-liberalism that has become the accepted economic orthodoxy. However, The onset of the global financial crisis in 2008 has been widely interpreted as a fundamental challenge to neoliberal governance, and there has been growing emphasis on the

political economy of financial deregulation and the vital role played by the global shadow financial system comprising tax havens, secrecy jurisdictions in stimulating illicit financial flows from Africa and other developing countries. Christian Aid (2009), for example, highlights that secrecy jurisdictions exploited the competitive deregulation of the financial markets over the last three decades by maximizing opportunities presented by the gaps emerging from the lack of national regulation of global finance. Inseparable from these tight networks is the role played by global banks in channelling resources outside Africa. The Global Witness (2009) highlighted a number of case studies, which focused on the nature of bank customers in Equatorial Guinea, Republic of Congo, Gabon, Liberia and Angola. In these countries, the national resource wealth has or had been captured by an unaccountable few. Nearly all of the banks doing business with these customers that featured in the Report are major international banks such as Barclays, Citibank, Deutsche Bank, and HSBC, all of which make broad claims about their commitments to social responsibility.

52. Another feature of international political economy in the recent decades is the increased demand for natural resources, notably oil, mining and other components of extractive industries and the emergence of Africa as important location for these resources. As shown in section two of this paper, the high concentration of IFF in extractive industries in Africa highlights its adverse impact on governance and politics in the continent. The large rents from mineral and energy extraction are facilitated by global financial liberalisation which allows assets to be hidden abroad as well as the large transnational movement of capital. The process of rent extraction reflects a close nexus between the interests, motives and actions of a number of actors, notably the political elite, multinational corporations and international banks. Especially in weak states, political elites act as gatekeepers between their jurisdictions and the global markets benefiting from the large rents extracted from natural resource exports, drug trafficking and other forms of illicit activities (Moore, 2012). In this business environment the ability of firms to survive does not depend merely on competitive advantage but on how they engage through market and non-market relations in a complex set of institutions. The ability of African countries to mobilize domestic resource is therefore enormously constrained by the lack of adequate transparency regulations. This raises the question of how these flows can be curtailed or at least reduced at both the source and at their intended destinations.

5.2 Governance and Illicit Financial Flows: Agreements and Conventions

53. There are various international conventions and agreements that aim to curtail the various forms of illicit financial flows. These conventions and agreements include the: (i) United Nations Convention against Corruption (UNCAC); (ii) United Nations Convention against Transnational Organized Crime; (iii) United Nations Model Double Taxation Convention between Developed and Developing Countries; and (iv) Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries⁵. There are also some initiatives headed by OECD with respect to tax issues. OECD has prepared a model bilateral agreement that requires transparency and exchange of tax information between the signing countries. There are also agreements between the EU and tax haven jurisdictions with regard to exchange of information on suspicious money transfers.

54. Following the September 11 2001 terrorist attacks on the United States of America (USA), several Western governments, regional and international institutions have taken various initiatives to combat money laundering. In October 2001, the USA enacted the USA PATRIOT Act (commonly known as the Patriot Act) to enhance the prevention, detection and prosecution of

⁵ Under the auspices of the United Nations Committee on International Cooperation in Tax Matters.

international money laundering and the financing of terrorism. The Act is primarily divided into three subtitles, with the first dealing primarily with strengthening banking rules against money laundering, especially on the international stage. The second attempts to improve communication between law enforcement agencies and financial institutions, as well as expanding record keeping and reporting requirements. The third subtitle deals with currency smuggling and counterfeiting, including quadrupling the maximum penalty for counterfeiting foreign currency.

55. Another example is the Financial Action Task Force on Money Laundering (FATF)-a 36-member inter-governmental body established by the G-7 in 1989 with the primary responsibility to coordinate international efforts on Anti-Money Laundering (AML)-assumed responsibility for Combating the Financing of terrorism (CFT). The FATF issued its first list of 40 recommendations on AML in 1990, and these have been revised twice (in 1993 and 2003) to take into account the changing global environment. The recommendations set out a basic, universally applicable framework of measures covering the criminal justice system, the financial sector, certain non-financial businesses and professions, and mechanisms of international cooperation (IMF, 2012). In the 2003 revision, the FATF also proposed an additional set of 8 Special Recommendations to reflect its new role on CFT following the September 2001 attacks. This set of "40+9" Recommendations is regularly used by the European Union (EU), the International Monetary Fund (IMF), the World Bank and other such regional/international institutions in their work on AML/CFT.

56. In the particular case of the European Union (EU), CFT efforts to have taken a two-tier approach: financial freezing measures and money-laundering legislation (Allam and Gadzinowski, 2009). Both sets of initiatives were introduced before the September 2001 attacks, but were later enhanced in the aftermath of the attacks. The financial freezing measures were implemented following the adoption of the UN Security Council Resolutions 1267 and 1373, thus establishing an EU system for targeting and sanctioning individuals and groups suspected of providing assistance, financial or otherwise, to any terrorist organization (Allam and Gadzinowski, *ibid.*). In the case of AML, the EU ensures implementation of the FATF 40+9 Recommendations with regard to financial sector regulation in its member states. To this end, the EU so far adopted three Directives on Anti-Money Laundering - in 1991 (91/308/EEC), in 2001 (2001/97/EC), and in 2005 (2005/60/EC). The Third Directive on the Prevention of the Use of the Financial System for the Purposes of Money Laundering or Terrorist Financing (2005) replaces the 1991 Directive.

5.3 Main challenges to Global Governance

57. The above mentioned initiatives are all in some way concerned with addressing illicit outflows. To this end, a variety of instruments are utilised, including standardisation, capacity building, regulations, and advocacy. While these initiatives are positive developments, much remains to be done. For example, a major issue is that some countries have not ratified the UNCAC and are therefore not required to cooperate with its mandates. Furthermore, loopholes in the international legal framework and differences between legislations in northern countries and Africa prohibit the effective investigation of IFF (Transparency International, 2011).

58. The magnitude and impacts of illicit financial flows on development raise the question of how these flows can be curtailed at both the source and at the destinations. One of the important barriers in the search for a global solution to combat this phenomenon is the lack of an institutional home for global governance, which can provide an outlet for policy debate and implementation.

59. Curtailing IFF requires concerted and simultaneous effort by both northern and southern countries. A two pronged approach based on more transparent and accountable legal and governance frameworks, as well as an integrated international asset recovery regime can help curtail IFF. The 2002 Monterrey Consensus highlighted domestic resource mobilisation as an essential element to sustain productive investment and enhance human development. However, demands at the Doha Conference in 2008 by the Task Force on the Development Impact of Illicit Financial Flows (which was led by Norway) to enhance the UN's Finance for Development process, especially boosting the capacity of the UN Committee of Experts on International Cooperation in Tax Matters, received little attention.

60. The repatriation of illicit funds under the present governance frameworks proved difficult and the practical investigations that are concerned with asset recovery are very complex. For example, stolen assets must be successfully identified in order to legitimately recover them under the UNCAC framework and international law. Even when the IFF are located, several hurdles complicate the effective return of these assets.

Box IV.1: The need for Effective Capital Repatriation Schemes in Africa

While African countries must address the loss of financial resources illicitly flowing to the west, they would be remiss not to consider how to reverse these flows. The primary challenge presented by IFF is the outflow of capital, which effectively serves to undermine development. Therefore, recuperating lost resources and providing mechanisms and incentives for their return will ultimately impact on economic growth and poverty reduction as governments recoup the resources to finance development projects. Ultimately, such a virtuous cycle could also help to reduce illicit outflows altogether. A number of countries in Asia and Latin America have already utilized such schemes with much success. For instance, Chile implemented the highly publicized mobilization of domestic resources through capital repatriation using debt-equity swaps. The outcome was greater investment and stronger economic growth rates. Even European countries have utilized capital repatriation schemes. In Italy, a tax amnesty scheme in favour of private foreign asset holders saw the inflow of US\$30 billion from Swiss banks. Fofack and Ndikumana (2009) suggest that capital repatriation would increase domestic savings, thereby leading to greater investment. They warrant that even a 25 per cent repatriation of all illicit funds accumulated up to 2004 would increase the average ratio of gross domestic investment to GDP from 18.5 per cent to 29.6 per cent (Fofack and Ndikumana, 2009).

The case of Sani Abacha, the former Nigerian Head of State provides a number of useful lessons to other African countries on effective strategies to track down and recover looted national assets. It represents the single most successful case of asset recovery by a State, where US\$ 2.3 billion of the illicit flows has been or is in the process of being recovered (see Maton and Daniel (2012)). Integral to the success of this case was the political will shown by the Government of Nigeria to carry out and follow up on the initial investigation by the law enforcement agencies. The process started with the establishment of an investigative process in Nigeria, followed by the cooperation of Switzerland as a lead offshore jurisdiction. Further, the case highlights the importance of utilizing civil asset recovery powers in conjunction with the compulsion powers of criminal law enforcing agencies

61. Indeed, there is also a lack of coordination between national and international agencies and the capacity of the former is often limited. Furthermore, there is a low level of expertise and experience in asset recovery and there is therefore a critical need for skilled accountants and specialized lawyers. Moreover, a lack of political will of both Western and African governments poses significant challenges to curbing IFF (Car, 2011).

62. The globalized nature of IFF has prompted a response that is generally associated with a number of non-governmental organizations such as Global Financial Integrity, Tax Justice and Christian Aid with the support of the Government of Norway.

63. Country-by-country reporting has been advocated by a strong non-governmental campaign as an effective means to combat the issue of transfer mispricing and it is now supported by the EU Parliament and Council of Europe (EUROCAC, 2011, Murphy, 2012). Under the full country-by-country reporting requirement, multinational corporations are to provide comprehensive information about their operations in each country, the names of all subsidiaries and affiliates; country-specific financial performance results; the tax charges included in their accounts; the cost and net book value of their physical fixed assets; and details of their gross and net assets. Further, the use of tax havens has been a central target of the non-governmental campaign which calls for adequate tightening of the regulations on tax heavens and secrecy jurisdictions

64. Another potential policy intervention is the strengthening of anti-laundering efforts based on existing initiatives. Efforts to curb money laundering will bring little fruit without effective control measures at both the origin and destination of these flows (Levi, 2012). Vital in the anti money laundering efforts is the strengthening of the capacity of African states, as stipulated in the *African Union Convention on Preventing and Combating Corruption*, to coordinate and harmonize the policies and legislation between State Parties for the purposes of prevention, detection, punishment and eradication of both crime and corruption on the continent. However, these efforts will bring little outcome if they are not accompanied by equal efforts at the destination countries. For example, one of the key priorities for the current Egyptian government is to recover an estimated US\$ 11b believed to have been transferred illicitly from the public purse during the era of the former President Hosni Mubarak. While many countries pledged support to help Egypt return the stolen assets, no monies have as yet been returned. According to reports by the Egyptian media and the BBC, officials at Egypt's Illicit Gains Authority claimed, after a recent trip to London, where some £ 85m (US\$ 132m) of assets remains frozen, that progress remains slow. They also complained that attempts to discuss the extradition of the former finance minister, from the UK back to Egypt where he has been convicted on fraud charges were refused.

65. The rise of a progressive agenda to curtail global IFF, especially on issues related to tax evasion, tax competition, and secrecy jurisdictions has been met with fierce resistance by a strong lobby of interest groups fighting to sustain the status quo. Lesage et.al (2010) highlights that the interests that stand in the way of a more progressive international tax agenda can be divided into two clusters:

- (i) The wealthy citizens and companies all over the world that profit from tax competition, tax avoidance, and tax evasion involving the 'offshore world' have become a basic feature of modern capitalism. A number of governments are reluctant to enter into open conflict with these powerful groups for ideological, electoral, and party-financing reasons;
- (ii) Several countries, with a vast financial sector applying secrecy, opacity and zero rates, have a direct interest in maintaining the status quo. This group not only includes certain small island economies, but also developed countries such as the US, Russia, and the UK.⁶

5.4 Africa's Response to Illicit Financial Flows

⁶ This does not preclude the fact that the US tries to curb tax-inspired capital export to protect its own treasury.

66. As highlighted in the above analysis, illicit financial flows have become a matter of major concern given the scale and negative impacts of such flows on Africa's development and governance agendas. This issue underscores the urgent need for a well-coordinated African response to guide regional and national policy-making, both in the design, as well as in the implementation of appropriate solutions. Moreover, African governments must be engaged at the international level to successfully overcome this challenge.

67. Awareness of this disturbing trend has been increasing as the adverse impacts on Africa's development become more apparent. Accordingly, regionally coordinated strategies are being instituted to help address the problem. For instance, the establishment of the High level Panel on Illicit Financial Flows from Africa, chaired by President Thabo Mbeki, was essentially a response to the urgent need for systematic changes at national, regional, and global levels through greater public pressure and sensitization to secure a strong African voice in the global arena.⁷

68. One of the main objectives of the high level panel is to develop effective regional and advocacy strategy to curtail IFF. The strong argument on the devastating economic and social impacts of IFF calls for a well designed advocacy and sensitization programme to ensure broad support in the fight against IFF. The success of this regional programme will be essentially based on the following preconditions: (i) strong political will from African leaders to prioritize the issue of IFF as a main development challenge and implement the policy recommendations arising from the programme; (ii) ensure that all stakeholders are fully apprised of the program's findings and recommendations; and (iii) the need to table pivotal issues before the various fora, and arm important stakeholders such as civil society organizations with evidence-based analyses that will allow them to carry out their own complementary advocacy activities.

69. The regional strategy can draw on some useful lessons from the campaigns against HIV/AIDS to enact change through raising awareness and building an African response and a broad consensus to curtail illicit financial flows from Africa. One powerful tool that could be used to secure change through public pressure and sensitization is to include it in the national education curriculum. As the former President of South Africa Nelson Mandela⁸ noted, 'Education is the most powerful weapon you can use to change the world.' However, to ensure sustainability of the regional programme against IFF, there is a critical need for a permanent champion responsible for the implementation and the follow up on the regional strategy and other aspects of the work of the High Level Panel on IFF. A good potential actor in this regard is the NEPAD Heads of State and Government Orientation Committee (HSGOC), which could provide leadership to the process, sets policies and priorities and implement the programmes of action.

70. The panel can also raise the awareness on the importance to improve institutional Frameworks for African Countries and the need to support sharing of good practices. For example, the African Peer Review Mechanism (APRM) can play a critical role in the domestication of the illicit financial flows agenda. The mandate of the APRM is to ensure that the policies and practices of participating countries conform to the values, principles, codes and standards enshrined in the

⁷The establishment of the High Level Panel (HLP) follows a resolution of the 4th Joint Annual Meetings of the ECA/AU Conference of Ministers of Finance, Planning and Economic Development in Africa in March 2011, which decided to address the debilitating problem of illicit financial outflows from Africa estimated at about US\$50 billion annually, in mandating the establishment of the Panel.

⁸ Mandela, N. (2003). Lighting your way to a better future; speech delivered by Mr. N. R. Mandela at the launch of Mindset Network.

Declaration on Democracy, Political, Economic and Corporate Governance, which are central factors in curtailing IFF. One possibility is to improve the APRM questionnaire and its constituent instruments to include the various components of illicit flows. The APRM could also encourage constructive peer dialogue and the sharing of information and common experiences in order to reinforce successful and exemplary practices among African countries.

71. Another recent landmark regional initiative, which places the fight against illicit financial flows at the heart of its agenda is the African Regional Anti-corruption Programme (2011-2016), established by the United Nations Economic Commission for Africa in collaboration with the African Union Advisory Board on Corruption (AUABC). It is encouraging to recognize that one of the priority items in the Regional Anti-Corruption Programme's is to strengthen stolen asset recovery. Moreover, the programme can play a key role in domesticating and streamlining the agenda on illicit financial flows and could effectively facilitate the engagement of the various stakeholders. This also applies to the African Tax Administrative Forum (ATAF), which was established in 2009. The forum can serve as a central platform to articulate African tax priorities, develop and share best practices in the region and build capacity in African tax policy and administration through peer learning and knowledge development.

72. Curtailing IFF requires concerted efforts by both northern and southern countries. This requires greater emphasis on regulating secrecy jurisdictions, strengthening anti-money laundering efforts, and enhancing the capacity of the UN Committee of Experts on International Cooperation in Tax Matters, among others. African leaders should seek strong political will from their western counterparts to support such initiatives as UN Resolution 55/188 on the illegal transfer of assets, as well as the Stolen Asset Recovery Initiative as a means to strengthen transparency in international financial transactions.

73. Africa's response to illicit financial flows will benefit from an African Convention on Transparency or a support to an international transparency convention. Such a convention should target the loopholes in the existing control regime, which places the burden of surveillance and enforcement costs of predatory behaviour and secrecy underpinning IFF on developing countries. The convention could also mandate retaliatory actions against the jurisdictions that undermine the laws and regulations of other jurisdictions

74. An initial step in the right direction would be to require greater transparency in the banking system, where banks are mandated to ascertain the identity, source of wealth, and country of origin of their depositors and their deposits. This would require the removal of the secrecy cloak which has helped tax havens flourish at the expense of African economies. There are numerous benefits to such a mechanism, including discouraging IFF, facilitating repatriation of stolen assets, as well as ensuring the payment of taxes to the appropriate government. To ensure compliance, the international rating agencies should be enabled to factor individual bank's "transparency performance" in assessing their credit ratings. Lower credit ratings ultimately impact shareholder profits and could therefore serve as a disincentive to facilitating IFF.

75. Going a step further, it would be extremely useful to require all firms (who should be registered with their respective Securities and Exchange Commissions (SEC) to regularly report on their employees, sales, financing, tax obligations, and payments on a country-by-country basis. Such glaring transparency would readily reveal any abuses linked to transfer pricing. African leaders may therefore also engage the G20 on such measures and may even help to develop a global system of mandatory information sharing on tax obligations and payments (Lowe, 2012). The EU

Savings and Tax Directive, Nordic, Canada and the United States of America already have such a mechanism in place for the automatic exchange of tax-related information.

VI. CONCLUSION

76. This parliamentary document has examined illicit financial flows from Africa as a major governance challenges and discussed their scale and developmental impact. The discussion of these cross-border transfers of illicit money, notably stemming from corruption, as well as corporate and criminal activities accentuate the detrimental impact on African development and governance.

77. The document has adopted a narrow definition of illicit financial flows, which defines these flows as money that is illegally earned, transferred, or utilized. It has essentially focused on the structural and governance limitations that fuel IFF from Africa. The term illicit financial flows underpin a different manifestation of the state-market relationship to that characterizing the conventional work on capital flight that follows standard mainstream neo-liberal models of utility and profit maximization by rational economic agents. The emphasis on criminal, corrupt and commercial activities of IFF underlines a policy response that encourages a more active role for the state and that highlights the need for a better regulatory environment via enforcement of national and global standards of financial transparency and democratic accountability.

78. The document highlighted that illicit financial flows create negative development impacts in Africa. These adverse effects are often complex and interdependent and have imposed detrimental economic, social and political consequences on African states. Certainly, these significant outflows of capital play a central role in undermining the potential for economic transformation on the continent. Moreover, illicit financial flows can result in large-scale corruption, and can contribute to the weakening of the state's capacity, while jeopardizing enforcement of the rule of law.

79. These huge outflows of capital play a significant role in undermining the potential for a developmental role of the state in Africa in the continent through draining tax revenues and scarce foreign exchange resources, stifling growth and socio-economic development, and weakening governance. The document underscored that the quality of public institutions has a major impact on capital outflow. Institutions play a very important role and have direct bearing on the management of the country's economy and as such, influence illicit financial outflows- either by curtailing the flows or by encouraging the repatriation of illicit capital.

80. Given Africa's need for a developmental state approach to unlock and mobilize the much need domestic resources for development, several strategies may be implemented to overcome the challenges of IFF on governance and development in Africa. First, the developmental state in Africa must have the political will and the necessary capacity. In addition, there must be a comprehensive development framework to combat IFF as opposed to short-term unregulated markets that characterized many African countries' economic management since the 1980s. Through this comprehensive development framework, governments will set out their vision for national and regional development – including, but not limited to the effective commitment to diversified economies, building capacity, and ensuring that all stakeholders are fully apprised of the illicit financial flows program's findings and recommendations – therefore providing policy certainty and predictability for social and economic agents at both national and regional levels.

81. The focus on hidden resources and their potential impact on development place the issue of illicit financial flows firmly in the broader realm of international political economy which emphasizes the role of governance at both the origin and the destination. This stands in sharp

contrast to the conventional models of capital flight, which tend to place the burden of the illicit financial flows on developing countries.

82. The magnitude and impacts of illicit financial flows on development raises the question of how these flows can be curtailed at both the source and at their intended destinations. One of the important barriers in the search for a global solution to combat this phenomenon is the lack of a global regulator to strengthen governance and help to stem the negative tide. A two pronged approach based on a more transparent and accountable legal and financial global governance as well as an integrated international asset recovery regime will go a long way in curtaling illicit financial flows from African countries.

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