# REPORT ON ILLICIT FINANCIAL FLOWS FROM AFRICA

## 1. Introduction

The COVID-19 pandemic, the war in Ukraine and the increasing costs of climate change and environmental challenges have had a particularly devastating impact on developing economies highlighting the critical need for addressing the financing gap. The ability to achieve the Sustainable Development Goals (SDGs) remains fragile when illicit financial flows (IFFs) continue to drain resources that are needed to fulfil human rights and pursue sustainable development. Domestic resource mobilization, assets recovery and curbing IFFs are more critical than ever. Governments' capacities to raise resources through return of assets will be fundamental to rescue the 2030 Agenda.

The 2030 Agenda identifies the reduction of IFFs as a priority area, as reflected in target 16.4: "by 2030, significantly reduce illicit financial flows and arms flows, strengthen the recovery and return of stolen assets and combat all forms of organised crime". This target is critical for financing efforts to achieve SDGs. IFFs were also identified as a global priority in the Addis Ababa Action Agenda (United Nations, 2015) on financing for development which calls for a redoubling of efforts to substantially reduce IFFs, with a view to eventually eliminating them.

The year 2015 witnessed the publication of a landmark report by the African Union (AU) – Economic Commission for Africa (ECA) High Level Panel on IFFs from Africa (the Mbeki Panel). The report (United Nations. Economic Commission for Africa, 2015), which was adopted by African Heads of State and government, assessed the volume and sources of IFFs from Africa. It shows that the most critical driving factor in the struggle to end IFFs is the political will of governments, in addition to technical capacity. The report firmly indicates the need for action in both sending and receiving countries. The use of the term by African heads of State and government on the global stage helped facilitate a wider dissemination of the concept.

The report by the Mbeki Panel shows that IFFs weaken state institutions by encouraging corruption and undermine the rule of law and the functioning of the criminal justice systems. The impacts lead to particularly dire effects for the most vulnerable. The United Nations Conference on Trade and Development (UNCTAD)'s Economic Development in Africa Report (EDAR) (UNCTAD, 2020) found that some countries with high IFFs spend on average 25 per cent less on health and 58 per cent less on education compared with countries with low IFFs. By eroding the tax base and discouraging public and private investment, they hamper structural transformation, economic growth and sustainable development.

Regardless of its importance, data on indicator 16.4.1, "total value of inward and outward illicit financial flows", are not yet reported as part of the SDG indicator framework (United Nations, 2017b). The world needs comparable and reliable statistics on IFFs to shed light on the activities, sectors and channels most prone to illicit finance, pointing to where actions should be undertaken as a priority to curb these flows.

After intensive global efforts by UNCTAD, the United Nations Office on Drugs and Crime (UNODC) and experts from member States and international organizations, globally agreed concepts for measuring

IFFs as SDG indicator 16.4.1 now exist. They were adopted by all member States represented at the Inter-agency and Expert Group on SDG Indicators (IAEG-SDGs), and the United Nations Statistical Commission, as well as endorsed at the political level by the FACTI panel (United Nations, 2021) and the Cluster V of United Nations Regional Commissions on Financing for Development in the Era of COVID-19 (United Nations, 2020). Selected methods to measure different types of IFFs have been pilot tested between 2018 and 2022 by 22 countries in Africa, Asia and Latin America, contributing towards refining global methods to measure IFFs and report on SDG 16.4.1.

This report presents the work to strengthen statistical capacities in African countries to measure tax and commercial IFFs within the United Nations Development Account (UNDA) project on "Defining, estimating and disseminating statistics on illicit financial flows in Africa". Tight cooperation of co-custodians of SDG indicator 16.4.1, UNCTAD and UNODC, enabled also other countries to benefit from their methodological support  outside the direct scope of this project: Egypt within the Integrated National Financing Framework (INFF) project, and Kyrgyzstan and Uzbekistan within the UNDA project "Statistics and data for measuring illicit financial flows in the Asia-Pacific region" coordinated by UNODC and the Economic and Social Commission for Asia and the Pacific (ESCAP).

## 2. Concepts developed and agreed

UNCTAD and UNODC, as custodians of SDG indicator 16.4.1 assigned by the General Assembly, have led the global methodological work to develop statistical definitions and methods to measure IFFs to support member States in monitoring progress towards target 16.4. In line with the General Assembly resolution (United Nations, 2017a) to ensure engagement with national statistical authorities, UNCTAD and UNODC established a Task Force on the Statistical Measurement of IFFs[1] in January 2019, involving experts from national statistical offices (NSOs), financial intelligence units, tax authorities, academia, non-governmental organisations, international organisations and other IFF experts.

As a result of this work, and for the purpose of the SDG indicator, UNCTAD and UNODC *Conceptual Framework for the Statistical Measurement of Illicit Financial Flows* (UNCTAD and UNODC, 2020) reflected the approved concepts and standards from the IAEG-SDGs, as designated by the United Nations Statistical Commission, and endorsed these concepts in a methodological proposal in October 2019. The methodological proposal reclassified indicator 16.4.1 from tier 3, indicating that no internationally established methodology or standards are available for the indicator, but methodology/standards are being (or will be) developed or tested to tier 2, meaning that the indicator is conceptually clear and based on internationally established standards, while data are not yet available from countries. Furthermore, the Framework was endorsed by the member States and international organizations at the 53rd Session of the United Nations Statistical Commission (UNSC, 2022) in March 2022.

[1] The Task Force is composed of statistical experts from Brazil, Finland, Ireland, Italy, Peru, South Africa and the United Kingdom, representing NSOs, central banks, customs or tax authorities. The Task Force also includes experts from international organisations with recognised expertise in this field. ECLAC, ESCAP, Eurostat, IMF, OECD, UNECA, UNSD, UNCTAD and UNODC are represented.

There is now a globally agreed definition of IFFs, which are defined as "*financial flows that are illicit in origin, transfer or use, that reflect an exchange of value and that cross country borders"* (UNCTAD and UNODC, 2020). The Framework identifies four main types of such activities (1) illicit tax and commercial practices, (2) illegal markets, (3) corruption and (4) exploitation-type and terrorism financing. According to this typology, the four main categories of IFFs are described as follows:

1. **Illicit tax and commercial IFFs**. This category includes illicit practices by legal entities as well as arrangements and individuals with the objective of concealing revenues, reducing tax burden, evading controls and regulations and other purposes. This category can be divided into two components:
    - IFFs from illegal commercial and tax practices. These include illegal practices such as tariff, duty and revenue offences, tax evasion, corporate offences, market manipulation and other selected practices. Some activities that are non-observed, hidden or part of the so-called shadow economy, the underground economy or the informal economy may also generate IFFs. Related activities included in the International Classification of Crime for Statistical Purposes (ICCS) comprise tax evasion, tariff, duty and revenue offences, competition offences, import/export offences, acts against trade regulations, restrictions or embargoes and investment or stock/shares offences.
    - IFFs from aggressive tax avoidance. Illicit flows can also be generated from legal economic activities through what is sometimes called harmful or aggressive tax avoidance (see box 1 for more detail on the distinction between legal and illegal illicit flows). Aggressive tax avoidance can take place through a variety of forms, such as manipulation of transfer pricing, strategic location of debt and intellectual property, tax treaty shopping, and the use of hybrid instruments and entities. For the purposes of the measurement of the indicator, these flows need to be carefully considered, as they generally arise from licit business transactions and only the illicit part of the cross-border flows belongs to the scope of IFFs.
2. **IFFs from illegal markets.** These include trade in illicit goods and services, when the money flows generated cross country borders. Such processes often involve a degree of criminal organisation aimed at creating profit. They include any type of illegal trafficking of goods, such as drugs and firearms, or services, such as smuggling of migrants. IFFs are generated by the flows related to international trade of illicit goods and services, as well as by cross-border flows from managing the illicit income from such activities.
3. **IFFs from corruption.** The United Nations Convention against Corruption (UNODC, 2004) defines acts considered as corruption, which are consistently defined in the ICCS. These include bribery, embezzlement, abuse of functions, trading in influence, illicit enrichment and other acts. When the economic returns from these acts directly or indirectly generate cross-border flows, they are considered IFFs.
4. **IFFs from exploitation-type activities and financing of crime and terrorism**. Exploitation-type activities are illegal activities that entail a forced and/or involuntary transfer of economic resources between two actors. Examples include slavery and exploitation, extortion, trafficking in persons, and kidnapping. In addition, terrorism financing and financing of crime are illicit, voluntary transfers of funds between two actors with the purpose of funding criminal or terrorist actions. When the related financial flows cross country borders, they constitute IFFs.

An important distinction is made to avoid double counting and link to the System of National Accounts (SNA) between two different stages leading to IFFs:

1. **IFFs linked to income generation**, as the set of cross-border transactions that are performed in the context of the production of illicit goods and services or the set of cross-border operations that directly generate illicit income for an actor during a non-productive illicit activity. Inward or outward IFFs occur when the operation in question is performed across a border.
2. **IFFs linked to income management**, as the set of cross-border transactions finalised to use the (illicit) income for investment in (legal or illicit) financial and non-financial assets or for consuming (legal or illegal) goods and services. If spent abroad, the operation is an outward IFF. If stemming from illicit activity outside a jurisdiction but is spent in the domestic jurisdiction, an inward IFF is generated.

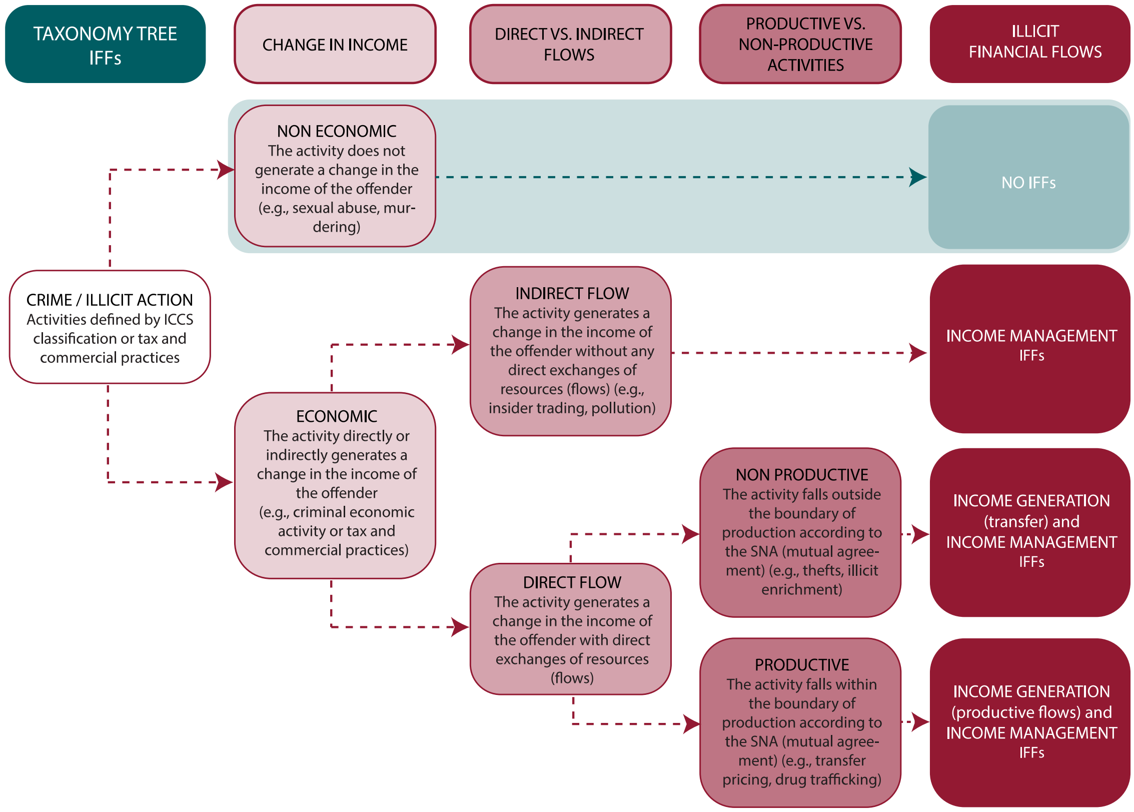
IFFs need to be classified using a discrete, exhaustive and mutually exclusive statistical classification aligned with existing statistical frameworks and principles. The ICCS (UNODC, 2015) is a good point of departure for identifying the activities that could generate IFFs. The ICCS does not cover all tax and commercial activities that may generate IFFs, for instance IFFs related to aggressive tax avoidance. Therefore, the classification of IFFs needs to be wider. A more exhaustive classification is being developed, where each activity is being analysed considering three aspects:

- Change in income: whether the activity is economic (directly or indirectly generating a change of income) or non-economic;
- Direct or indirect flows: activity generating a change of income with or without direct exchange of resources;
- Productive or non-productive activities: falling within or outside the production boundary as defined in the SNA.

Such taxonomy (see

Figure 1) allows for addressing not only whether each activity generates IFFs, but also which part, i.e., income generation or income management, thus guiding IFF measurement.

*Figure 1. The decision tree for IFF taxonomy*




*Source: (UNCTAD, 2022a)*

## 3. Statistical methods pilot tested

IFFs are deliberately hidden and, as they take many forms and use varying channels, their measurement is challenging both conceptually and in practice. UNCTAD and UNODC, therefore, provide different methods for the measurement of different types of IFFs. The measurement challenges also differ across countries, depending on main types of IFFs affecting the country, data availability, mandates of national institutions, statistical capacity and national policy priorities. Thus, a suite of methods is suggested for selection allowing country-specific solutions and the flexible application of the most suitable methods in each country.

In May 2021, *Methodological Guidelines to Measure Tax and Commercial Illicit Financial Flows* (UNCTAD, 2021) were published for pilot testing. They identify a suite of methods for the measurement of the main types of tax and commercial IFFs for pilot testing. The guidelines put preference on bottom-up and direct measurement of IFFs based on using all microdata available to national authorities.

The *Methodological Guidelines* are aimed at statistical and other national authorities with a mandate to collect and access detailed data. Microdata available to national authorities enable the compilation of more reliable estimates. However, simpler methods are proposed in parallel with more sophisticated methods to enable IFFs' estimation also where less data are available. The UNCTAD guidelines provide two methods for each of the three main types of tax and commercial IFFs:

1. **Trade misinvoicing by entities**
    - Method #1 - Partner Country Method Plus
    - Method #2 - Price Filter Method Plus
2. **Aggressive tax avoidance or profit shifting by multinational enterprise groups (MNEs)**
    - Method #3 - Global distribution of MNEs' profits and corporate taxes
    - Method #4 - MNE vs comparable non-MNE profit shifting
3. **Transfer of wealth to evade taxes by individuals**
    - Method #5 - Flows of undeclared offshore assets indicator
    - Method #6 - Flows of offshore financial wealth by country

Partner Country Method Plus (method #1) reviews bilateral discrepancies in reported trade flows, i.e., what country A reports as its imports from country B is cross-checked against country B's exports into country A. The challenge of multiple and varying reasons for these discrepancies, such as valuation and partner country attribution, but also trade systems in place and others, are addressed step-wise in the method to identify the amount of asymmetries to be contributed to IFFs. This approach is made possible by exploiting the detailed trade flows data available within national statistical system from national and bilateral partners Customs Authorities.

Price Filter Method Plus (method #2) builds on identifying abnormally priced transactions in international trade by first designing the price filter and then identifying abnormally priced transactions, to identify signs of IFFs. The method uses granular, transaction-level microdata and does not rely on partner's transaction data. Limitations and uncertainties of the method are partially offset by involvement of national Customs experts.

Global distribution of MNEs' profits and corporate taxes (method #3) looks at the distribution of profits of an MNE among its units globally and relates it to the corresponding corporate (effective) tax rates and underlying economic activity of a particular unit. It assumes that an MNE unit is likely to shift profits out of the country if another unit's tax regime induces a lower tax rate. Depending on data availability, using unit-level microdata may produce the most reliable estimates of profit shifting by MNEs.

MNE vs comparable non-MNE profit shifting (method #4) compares units belonging to MNEs with comparable domestic (non-MNE) units to identify potentially tax-avoiding behaviours, and then determine the amount of profit shifted as a measure of IFFs. The method is based on business statistics microdata that are available to statistical authorities in many countries, although it may be tricky to fully implement in small economies where the number of business is lower.

Flows of undeclared offshore assets indicator (method #5) looks at undeclared offshore assets, essentially by comparing what has been declared by citizens of a country A and what internationally reported data say about these assets held abroad by citizens of country A. Assumptions are required to transform stock measures into flow measures to approximate outward IFFs for a country. This method's data requirements are significant.

Flows of offshore financial wealth by country (method #6) starts from global level imbalance between international portfolio liabilities and assets, thus identifying global offshore financial wealth. This is then broken down by country of ownership and by International Financial Centre, and finally, assuming the non-compliance rate on offshore wealth to identify the level of illicit flows. Again, transforming stock into flow measure is required and similarly to previous method, also here data (un)availability is a significant challenge.

The above methods are tier classified, allowing member States to exercise flexibility and select a feasible method. A three-tier classification is proposed, with tier 1 as the preferred method based on the soundness of methodology, data requirements, and expected quality of estimates. Tier 2 is proposed as a fallback option if tier 1 method cannot be applied. If neither are applicable, a tier 3 method could be used. Generic results of the classification exercise of the suggested six methods are presented in Table 1 with more detailed information available in *Methodological Guidelines* (UNCTAD, 2021).

*Table 1. Tier classification of suggested methods*

| Group | Method | Soundness | Source data | Results | Overall | Tier class |
|---|---|---|---|---|---|---|
| Trade misinvoicing by entities | #1 Partner Country Method (PCM+) | 11 | 11 | 12 | 34 | 2 |
| | #2 Price Filter Method (PFM+) | 14 | 15 | 15 | 44 | 1 |
| Aggressive tax avoidance or profit shifting by MNEs | #3 Global distribution of MNEs' profits and corporate taxes | 12 | 8 | 9 | 29 | 3 |
| | #4 MNEs vs comparable non-MNEs | 13 | 14 | 14 | 41 | 1 |
| Transfer of wealth to evade taxes by individuals | #5 Flows of undeclared offshore assets indicator | 9 | 10 | 10 | 29 | 3 |
| | #6 Flows of offshore financial wealth by country | 8 | 9 | 10 | 27 | 3 |

*Source: (UNCTAD, 2021)*

UNODC has developed and continues to enhance methods to address IFFs from criminal activities, such as smuggling of migrants, drugs trafficking, illegal mining, wildlife trafficking, and corruption, providing guidance and expert support to national authorities undertaking measurement. Guidelines, tested for smuggling of migrants, trafficking in persons, wildlife trafficking, and drugs trafficking encompass data sources mapping, streamlining data collection processes and defining data collection strategies, conducting practical exercises and guiding institution in work on data collection. The approach taken by UNCTAD and UNODC considers the multi-dimensional nature of IFFs, identifies the main types of IFFs to be measured and lays out a framework in line with existing statistical definitions, classifications and methodologies, in particular with the SNA and Balance of Payments (BoP). Work by custodian agencies continues to develop a comprehensive classification of IFFs and design methods to aggregate various types of IFFs into a single indicator on IFFs, towards measuring and reporting on SDG indicator 16.4.1.

Important element of development and refinement of methodological guidelines to measure IFFs, both from criminal side and tax and commercial, is the pilot testing of proposed methodologies and related tools. Pilot studies focus first on types of IFFs that are most prominent in a country and for which data are available. Coverage of different IFFs will be improved gradually along with data improvements. A series of pilot studies have been conducted with partners, UNODC and relevant UN Regional Commissions, in 22 countries to date. The pilots have provided or continue to provide critical information for refining statistical methods to measure IFFs, either in terms of modifying the methodological approach (e.g., due to unreliable quantity information in trade statistics, related proposed reliability weighting procedure for Partner Country Method Plus on trade misinvoicing turned out to be unattainable in parts), or proposing alternative avenues (e.g., inspecting remittance flows), or clearly specifying national adaptations in applying methods. Further refinements are expected after current pilot testing concludes towards the end of 2022.

The first pilots carried out in Latin America between 2018 and 2020, by UNODC, show the way forward for other countries. In the first pilots, Columbia, Peru, Ecuador, and Mexico measured IFFs from selected illegal markets, such as drugs trafficking and smuggling of migrants. Estimates in Mexico, for instance, show that an inflow of IFFs equivalent to around $12 billion was generated annually by drug trafficking activities conducted between 2015 and 2018.

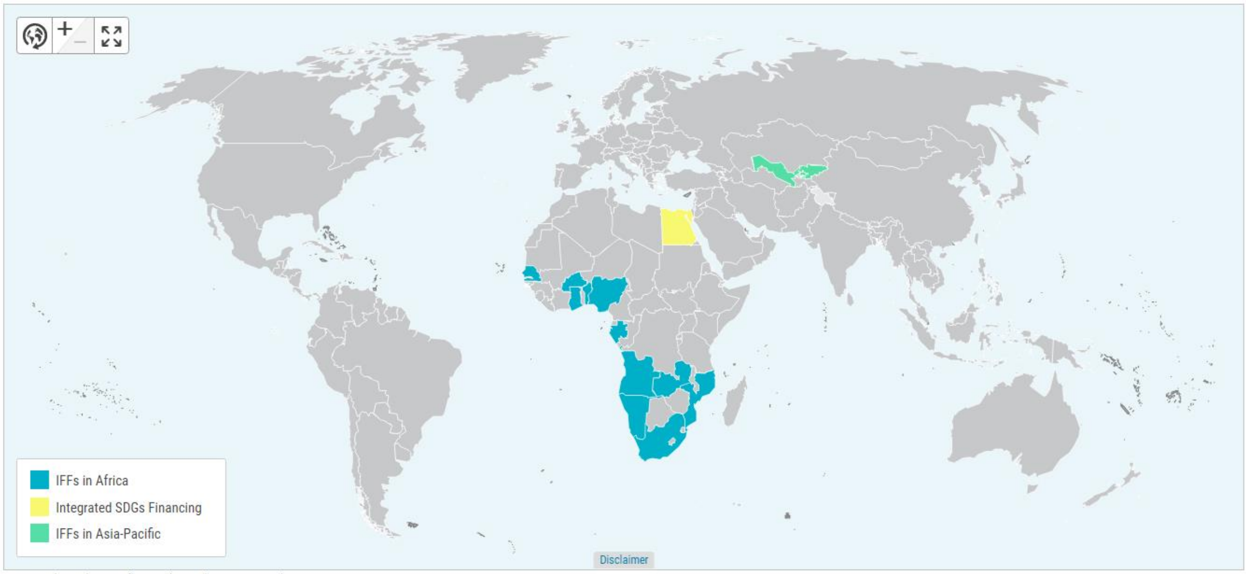
Similarly, inward IFFs from cocaine trafficking were estimated for Peru ($1.48 billion annually between 2015 and 2017) and Colombia (range: $1.5 billion - $10.2 billion for 2019). Smuggling of migrants is instead estimated to have generated an annual average of $1.1 billion in inward IFFs for Mexico and $13.6 million outward IFFs for Ecuador (2016-2018 data). Pilots also addressed the measurement of IFFs from illegal gold mining and trafficking in persons, even if data in such cases did not allow for a sufficiently robust estimate.

Tax and commercial IFF Methodological Guidelines have been or are being tested in 14 countries in Africa and Asia (see Figure 2):

- The United Nations Development Account project on Defining, estimating and disseminating statistics on illicit financial flows in Africa, includes eleven countries[2] and co-led by UNECA;
- The United Nations Joint Fund Support on Integrated SDGs Financing with Egypt and,
- The United Nations development account project on Statistics and data for measuring illicit financial flows in the Asia-Pacific region with two countries[3] measuring tax and commercial IFFs (and four countries crime-related IFFs). This project is implemented with ESCAP and UNODC.

[2] Angola, Benin, Burkina Faso, Gabon, Ghana, Mozambique, Namibia, Nigeria, Senegal, South Africa, Zambia.
[3] Kyrgyzstan and Uzbekistan.

Figure 2. Pioneering countries measuring tax and commercial IFFs, by project




Source: (UNCTAD, 2022b)

# 4. Process of pilot studies

Effective policies to curb IFFs require reliable and granular IFF statistics, tailored to national circumstances. Part III of the Methodological Guidelines (UNCTAD, 2021) provides concrete and operational recommendations for national statistical authorities, NSOs and other compilers of official statistics for the measurement of tax and commercial IFFs. It provides guidance on steps to take to start compiling estimates of tax and commercial IFFs.

First, it suggests a consideration of national circumstances, information needs and prominent types of IFFs. These can also help identify relevant stakeholders, as it is important to map out the national system of relevant authorities to organize the necessary collaboration to measure IFFs. It may be as useful to identify the relevant authorities and stakeholders before conducting an IFF risk assessment to seek their input on the assessment from the outset. These steps could be reversed, intertwined, or processed in iterations.

This enables the review of data availability and selection of data sources across agencies to capture the most prominent types of tax and commercial IFFs. A tier classification of methods considers national setup and capacity, existing data sources and related methods used in official statistics, legal and regulatory frameworks, and other criteria. This guides the selection of method to measure IFFs. Often an operational definition of IFFs is needed to meet the national data needs and ensure feasibility considering available data, methodology and capacity.

The definition is influenced by which methods is used (again, also the reverse holds, these processes being intertwined, running in parallel, and/or in iterations). Compilation and dissemination of IFFs statistics require some consideration due to the requirements of SDG reporting. Finally, we give a listing of practical recommendations to NSOs in their work in coordinating and/or compiling tax and commercial IFFs. These steps are outlined in Figure 3 and further elaborated below.

## The measurement journey

*Figure 3. Schematic presentation of steps to measure IFFs*


*Source: UNCTAD and ECA*

**Step 1: Self-assessment questionnaire to prepare for the measurement of IFFs**
As the types and extent of illicit financial flows differ in each country, it is essential to assess the country's unique situation before starting the measuring journey. A useful first step is to conduct an IFFs risk assessment to review existing statistics and information to fully understand the national circumstances. This type of analysis is a crucial first step as it highlights priorities and challenges and allows the pilot project team to tailor the measuring process to suit the needs of that particular country.

**Step 2: Mapping of national agencies and their roles**

It is vital to identify and involve the relevant national institutions and agencies in the measurement process to ensure the correct technical skills are available and a variety of perspectives are considered. Organisations may include the national statistical authority; policy-making bodies; tax and regulatory bodies; financial intelligence centres or intelligence and security services; law enforcement and prosecutorial authorities; ministries of foreign affairs and trade, chambers of commerce; international and foreign partners; non-governmental organisations and academia.

**Step 3: Data availability and quality review by method**

This step involves determining what data is available and assessing the quality and usefulness thereof. As illicit financial flows are clandestine in nature, accessing accurate data is often a challenge and should be factored in when undertaking a statistical measurement process. The availability of data also determines which flows can be measured and which methods are chosen, thus affecting the next steps in the process.

**Step 4: Method selection**

The selection of a method is based on the availability and quality of data in a specific country. A tier-classification assessment is suggested to choose the most appropriate method based on the national circumstances. Method fact sheets have also been made available to further refine the process of selection. Where possible, it is recommended that more than one method is applied when estimating and measuring illicit financial flow to confirm the reliability and robustness of the results.

**Step 5: Pilot testing plan and operational definition**

National statistical authority, with input from experts and stakeholders, must draw up a pilot testing plan based on the country's specific circumstance. As measuring all the IFFs in a country is a near-impossible task, the focus should be on identifying the most prevalent and detrimental types of flows and most crucial data needs of that particular country. An operational definition is a clear, concise and detailed description of what an indicator is attempting to capture.

**Step 6: Compile and disseminate IFF statistics**

This step involves testing the chosen measurement methods with the available data one or two aspects or sectors to produce initial estimates of the flows. Through iteration and testing, the process can then be refined until it is possible to conduct an in-depth and comprehensive analysis of the illicit financial flows at country level. Estimates can be shared with other participating pilot countries and later published in a clear and transparent manner at an appropriate time.

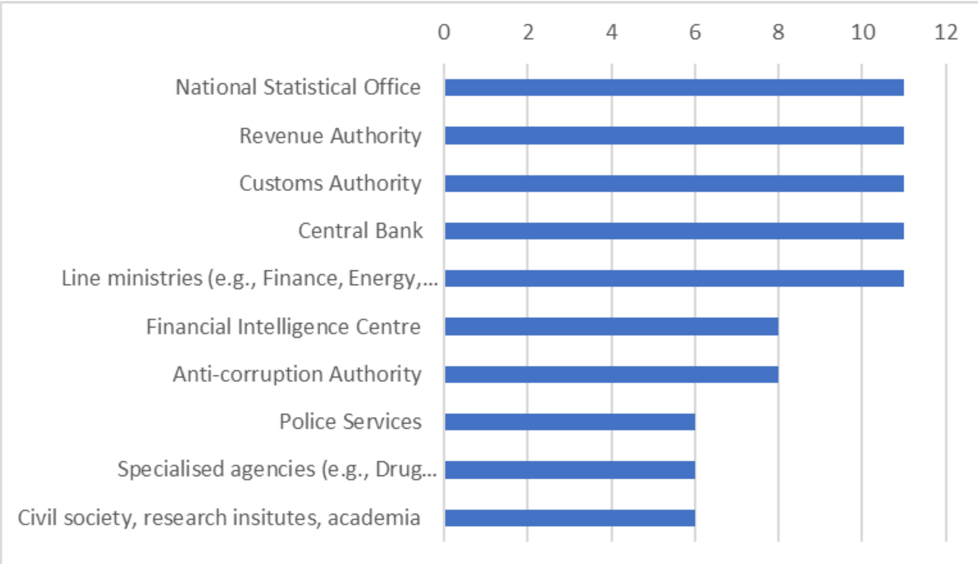
# 5. Findings from pilots

## National ecosystems to track IFFs

As noted earlier, the methods to measure tax and commercial IFFs have been tested by fourteen countries in Africa and Asia. This section focuses on pilot testing processes in eleven African countries within the United Nations Development Account project on IFFs in Africa (see Figure 2), namely by Angola, Benin, Burkina Faso, Gabon, Ghana, Mozambique, Namibia, Nigeria, Senegal, South Africa, and Zambia.

Each pioneering country has formed a Technical Working Group (TWG) consisting of the relevant national stakeholders either from the perspective of data, technical expertise, or knowledge to address IFFs. These Inter-Agency Groups often consist of the central bank, ministry of finance, revenue and customs offices, tax authorities, relevant ministries, financial intelligence units, Civil Society Organisations (CSOs), etc. The composition depends on the national institutional setup. IFFs leave traces in many administrative and statistical records. The data scattered across various institutions need to be pooled together to estimate IFFs. To ensure provision of objective and neutral information for SDG indicator 16.4.1 on IFFs, reporting on SDG indicators is coordinated by the NSO of each country in line with the General Assembly resolution A/RES/71/313 (United Nations, 2017a) and the Fundamental Principles of Official Statistics (United Nations, 2014). The coordination role of the NSO enables national institutions to come together and collaborate in a coordinated manner to compile comprehensive, reliable and high-quality statistics on IFFs. Figure 4 reflects the institutions involved in the IFF measurement pilots.

*Figure 4. The number of institutions involved in measuring tax and commercial IFFs in countries*




*Source: UNCTAD and ECA*

## Data availability

National statistical systems already have some of the data needed for the measurement of IFFs, but these data are scattered across a range of authorities and domains. For instance, existing national accounts and balance of payments statistics include estimates of illegal economic activities and the non-observed economy; they provide a good starting point for the measurement of IFFs. Relevant data may be held by the police and ministries and councils of justice, financial intelligence units and other government agencies collecting information on seizures and criminal offences. In addition, tax authorities collect relevant data for assessing the tax gap, and they exchange country-by-country reporting data on multinational enterprises. Customs' data and statistics on international trade in goods and services provide useful information on commercial IFFs.

Over 60 per cent of NSOs collate relevant data on underground, illegal and informal activities using surveys, administrative sources, mirror statistics, international studies and expert assessment (IMF, 2018). While these activities are largely domestic, many of them also generate cross-border flows. There are also systematic data collections on crime and related IFFs; UNODC, for instance, compiles statistics on drugs as reported directly by countries, including detailed data on demand, supply, prices, drug characteristics, seizure data, etc.

Compiling statistics on IFFs requires access to many data sources held by different authorities. Central banks, customs, tax authorities and NSOs often have the strongest mandate to collect and access such data. Several global databases also contain relevant data for the compilation of IFF estimates, for instance the OECD country-by-country reporting data, UNCTAD Global Transport Costs Dataset for International Trade, the United Nations Comtrade database and the locational banking statistics by the Bank of International Settlements.

Measuring IFFs requires close collaboration within the national statistical system and with administrative data providers. The compilation of SDG indicator 16.4.1 is a technical, statistical activity to be based on statistical considerations only in line with the Fundamental Principles of Official Statistics (United Nations, 2014). NSOs, as the focal point for coordinating the compilation of SDG indicators, should lead and coordinate the work to bring the necessary stakeholders together to measure IFFs.

During the closing event in Addis Ababa, in June 2022, countries have shared their experience and lessons learned concerning the data mapping, as shown below:

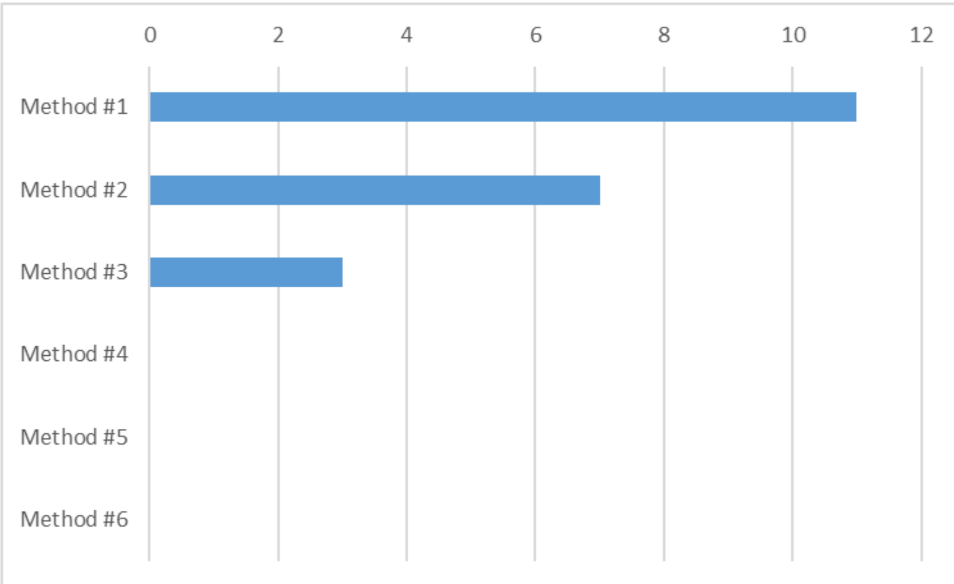
- In most countries, international trade data are available at least at certain level of disaggregation rendering them suitable mostly for application of method #1, whereas transaction-level trade data are sometimes incomplete, specifically referring to the quantities, not supporting their suitability to apply method #2.
- Access to data, both at national (Customs) and international (UN Comtrade) levels is a challenge for several countries, depending on the structures in place in countries.
- Business registers and detailed enterprise statistics are scarcely available for MNEs' units operating in countries; moreover, linking various national registers and statistical databases is hindered in several cases, rendering the application of methods #3 and #4 unattainable.
- Data availability at required granularity levels (usually microdata level) for several methods, notably methods #2, #3, #5 and #6 are not available to officials measuring IFFs in many countries.
- Data and statistics exchange within and across countries is mostly non-existent, disrupting many processes of identifying and measuring IFFs.
- Data confidentiality is also a challenge affecting the measurement work. Sub-committees within TWGs should be established to work on the specific measurement methods, based on where the data reside, thus potentially addressing confidentiality issue.
- There are no guidelines on data cleaning. Furthermore, it was highlighted that data cleaning and analysis is linked to data quality and is an iterative process and not linear. Moreover, national statistical infrastructure and capacity will dictate these inherently country-specific processes.
- It is important for countries to produce comprehensive data. Countries need to put more efforts towards improving their national statistics generally, in particular trade and customs statistics

## Types of IFFs measured and methods tested

UNCTAD invited pioneering countries to test one or two methods to measure IFFs. All 11 pioneering countries tested Method #1 – 'Partner Country Method Plus' and 7 countries tested Method #2 – 'Price Filter Method Plus' to measure trade misinvoicing (see Figure 5). The selection of methods is based on data availability for national institutions. Three countries tested Method #3 to measure aggressive tax avoidance by MNEs. Most countries are interested to pilot test other methods in their follow up work.

The first findings show that the methods on aggressive tax avoidance by MNEs and method on tax evasion by individuals are the most challenging methods as they require better availability of granular data. Moreover, specific economic and market conditions may limit the choice of methods, e.g., specific prominent sectors (e.g., mining) being fully dominated by multinational enterprises, whereby no domestic units could be identified to use a control group. All participating countries prepared national action plans to guide further work and donor support; and the feedback will help UNCTAD refine the methodological guidelines for global use.

*Figure 5. Methods tested by countries to measure tax and commercial IFFs*




*Source: UNCTAD and ECA*

Furthermore, pilot countries have expressed their feedback on the use of the Guidelines as per below:

- Guidelines, methods, and concepts were clear, helpful and contributed to awareness raising and stakeholder engagement. But the Guidelines should be more practical, user-friendly and in an abridged volumes format.
- Methods, where possible should be automated, capacitating customs and statistical officials to use the information from an intelligence perspective to curb IFFs at a tactical and operational level.
- Timeframe of the project allowed for limited pilot testing of methodologies, hence only a few have been selected (coupled with above-mentioned data availability issues).
- Methods #1 and #2 should be used as complementary methods (also aligned with tier-classification of methods, see Table 1).
- Training and pilot process were very helpful in contributing to stakeholder engagement, creation of governance structures to measure (and curb) IFFs.

## Experience and lessons learned

Preliminary results of pilot testing activities confirm the feasibility of the task, yet challenges in coordinating access and use of data, the collaboration between several entities and the estimation exercise remain. Early feedback shows that support by national consultants, training provided by international organizations and integration of national institutions into the TWG, are crucial for compiling statistics on IFFs, all this was further complicated by the COVID-19 restrictions in 2021-2022.

Some countries expressed that the piloting timelines were very limited, coupled with competing demands which impacted on the production, approval/validation and publication of the results. The measurement work needs to be formalised and endorsed at the political level, with officials making this part of their day-to-day activities. Incorporation into the daily activities renders this work sustainable. Nevertheless, the outcome from countries estimations is a milestone and an initial important step towards further efforts to validate, refine and publish results.

A few countries shared their preliminary results during the closing event, while others still needed to validate their results through their various governance structures.

Preliminary findings in Burkina Faso indicated IFFs in the export trade. For instance, in the gold sector, illicit transactions occur between Burkina Faso and Uganda, as well as with Switzerland. Other commodities have also been identified as prone to IFFs, such as zinc, sesame, beverages, or fuels.

In Namibia, the pilot study analysed illicit flows related to trade misinvoicing and revealed substantial amount of illicit finance leaving and entering the country related to six selected commodities: diamonds, diesel, petrol, gold, uranium, and fish.

Nigeria, on the other hand, studied the global distribution of MNEs' profits and corporate taxes to gain a better understanding of profit shifting, where the petroleum sector is mostly affected by IFFs. The results showed that profits are remitted to different countries mostly in tax havens. Some MNEs exclusively make transfers to affiliates in countries that fall in the vulnerability category, implying that such MNEs only make transfers to affiliates in tax havens.

A few countries decided not to share their results at the moment due to the confidentiality and sensitivity of the results/information. Gaining more experience and continue to strengthen their capacity and robustness of the estimates will increase their reliability upon their public dissemination. Transparency being a key to addressing IFFs at national and international levels, efforts to encourage sharing results and publishing official statistics on IFFs are expected by both, national and international agencies.

Nonetheless, the following can be observed based on the work and preliminary results from the eleven pilot countries:

- Most countries seem to have identified extractive industries (e.g., mining of gold, diamonds, or copper; fishery; oil industry) as the activities most prone to tax and commercial IFFs, both trade misinvoicing and MNEs profit shifting.
- Moreover, in several countries specific economic and market conditions also limit the application of certain methods, e.g., specific prominent sectors (e.g., mining) being fully dominated by MNEs, whereby no domestic units could be identified to use a control group.
- Although extractive industries seem to be mainly targeted and hardest hit by IFF outflows, other areas of tax and commercial IFFs have also been identified (e.g., other machinery). Highest values reported amount of IFFs up to more than 60% of total trade, in some cases even up to nearly a fifth of national GDP, although the estimates are still in a very preliminary phase and require further verification.

- This has also been outlined by pilot countries to ensure iterations in estimation processes and make small refinements to the measurement of IFFs (within the guidelines), creating learning Communities of Practice that contribute to the adaption of the methodological guidelines.
- Sharing of information between authorities within countries (inter-country) is critical and was flagged as an important lesson. Equally, sharing information among countries (extra-country) is critical to understand the risks, trade data disparities which are important to inform institutional interventions for curbing IFFs. This includes sharing information with pilot countries through a Community of Practice at the bi-lateral, regional and global level.
- A Community of Practice on IFFs was recommended among pilot countries as a platform for countries to be able to learn from each other, share information and best practices on curtailing IFFs regarding particular sectors and countries, or on data issues and the various methods, etc. Also, a few countries developed Sub-Committees to address the various measurement methods or focus on particular sectors, statistical or economic matters. Sub-Committees represent a useful lesson that can be used to focus on specific measurement methods, addressing data confidentiality issues, or specific projects or content etc.
- Moreover, resources need to be allocated to ensure that these TWGs on the measurement are made permanent. There is a need for continued capacity building and support through the technical expertise from the UNECA, UNCTAD and UNODC (and their experts). This affects the sustainability of the work going forward.

## 6. Further work in countries and globally

While some elements of IFFs are more readily measurable, others are highly challenging to estimate, including bribery, abuse of functions, illicit enrichment and illicit tax practices. Country pilots are central to building the capacity to measure IFFs and testing the feasibility of measurement. Experience gained during the country pilots show the way forward on tackling the measurement of IFFs.

There is a need for continued capacity strengthening and support through the technical expertise from the UNECA, UNCTAD and UNODC (and their experts). Further technical support is required in terms of training for the responsible authorities to strengthen their capacities, in order to measure and monitor IFFs, and training panel of national experts on the different methods of assessing IFFs to ensure the production of annual monitoring reports for SDG indicators 16.4. Financial support to acquire computerized software equipment which will improve the performance of data systems and continued capacity strengthening for long-term assistance in statistical training of national experts is also needed. Further steps also encompass technical and financial support in dissemination of results, securing sensitive data, sensitization and awareness raising at high level government forums and other stakeholders.

The measurement work needs to be formalized and endorsed at the political level, incorporating the work into daily activities of government officials renders this work sustainable. Moreover, resources need to be allocated to ensure that TWGs' work on measurement is made permanent.

Measurement of IFFs is the first step in identifying threats and risks from IFFs. This work needs to continue and expand, with further steps covering also conducting a country risk profile on the IFFs, which will inform the policy processes to curb IFFs. Such work also envisages partnering with African Union Commission (AUC), the African Tax Administration Forum (ATAF), the African Development Bank (AfDB), the Tax Justice Network-Africa (TJNA), the African Union High Level Panel on IFFs, and similar stakeholders globally and in other regions.

The early pilots developed tools and approaches and tested first methods to measure IFFs. As a result, refined tools and methods can be made available for all interested countries to use globally. In order to raise awareness, UNCTAD has published its annual SDG Pulse (UNCTAD, 2022a) reviewing the work completed up to now on the statistical measurement of IFFs and its pilot testing, as well as launched its first UNCTAD In Action (UNCTAD, 2022b) piece on IFFs. The latter shows measurable results of the implementation of projects on the measurement of IFFs.

UNCTAD and ECA have also participated in several events presenting the outcomes of the project with numerous stakeholders. The Closing Conference of the pilot activities organised in June 2022, in Addis Ababa, provided the first platform for pioneering countries to share their experience and lessons learned with external parties such as AUC, ATAF, TJNA, to name a few. Furthermore, a panel discussion on illicit financial flows shared the first outcomes of pilots with the international community at the UNCTAD 2nd Illicit Trade Forum, in September 2022, in Geneva. The panel discussed experiences and lessons learned in Egypt and Zambia, as well as regionally in Africa and Asia. Delegates congratulated countries for their pioneering work in this very challenging area and emphasized the importance of high-quality information for more targeted and effective policy action. Moreover, a breakaway session was organised during the 10th Pan African Conference on IFFs and Taxation in September 2022, in Lusaka, Zambia. Zambia and Namibia presented their experience and first results of the estimation process to other countries' representatives and African and International non-governmental organisations (NGOs) raising awareness on the need to provide Governments with quality estimates for policy actions.

In addition, a global UN capacity development project will start in 2023, relying on methodological support, guidance and training by UNCTAD and UNODC. It will be carried out in coordination by UNECA with all UN Regional Commissions. The project will enhance the capacity of developing countries across regions to measure and curb IFFs, enhance investigative and analytical capacities and improve domestic resource mobilisation to strengthen socio-economic resilience to pursue the 2030 Agenda.

UNCTAD and UNODC invite all interested countries to test the measurement of IFFs that affect their economies the most. Estimating IFFs will not only provide clarity on the scope of IFFs, but also help improve the quality of key macroeconomic statistics, such as GDP, by improving their coverage and exhaustiveness.

Furthermore, estimating IFFs will also help improve policy agenda and actions towards reducing economic inequalities and reinforcing fundamental human rights for all. IFFs are perpetually endangering human rights such as the right to social protection, to an adequate standard of living and to the highest attainable standards of physical and mental well-being; the right to education and the enjoyment of benefits of cultural freedom and scientific progress; to right to equality before the law; the right to work in just and favourable conditions; and to freedom of opinion and expression, to name a few.

Extreme poverty is creating a marginalized population who has no access to basic human rights. When wealth is illicitly transferred abroad, it directly impacts countries' growth and job creation (Shubert, 2015). National expenditures in social services, health care, as well as education are threatened. African countries, for example, with high IFFs are deemed to spend on average 25% less on health and 58% less on education (UNCTAD, 2020).

Tax evasion, tax avoidance and all other mechanisms depriving tax revenues of countries are violating fundamental human rights, and more specifically, women's rights. The COVID-19 pandemic has been exacerbating the living conditions of women around the world reinforcing the inequalities of their unpaid care and domestic work. National governments, mostly in the global south, lacking these revenues, exacerbated by the presence of IFFs, are deprived of investing in public services tackling gender inequalities and poverty (ActionAid International, 2022).

The statistical Task Force will continue its work to support countries in the pilot testing of the measurement of IFFs with a view to developing a global *Statistical Framework for the Measurement of Illicit Financial Flows* with practical and methodological guidance in line with the *Conceptual Framework*. This will include a classification of activities generating IFFs, linked to the SNA and BoP concepts, and recommended methods to measure different types of IFFs in SDG indicator 16.4.1.

Further work will also aim at developing nuanced measurement of IFFs to support policy action and at the same time developing methods to aggregate estimates of different types of IFFs into one SDG indicator, e.g., to adjust for double counting. In the future, the measurement of IFFs as a satellite account taking into consideration national accounts concepts and definitions could be worth exploring.

# 7. Recommendations and tools for measuring IFFs

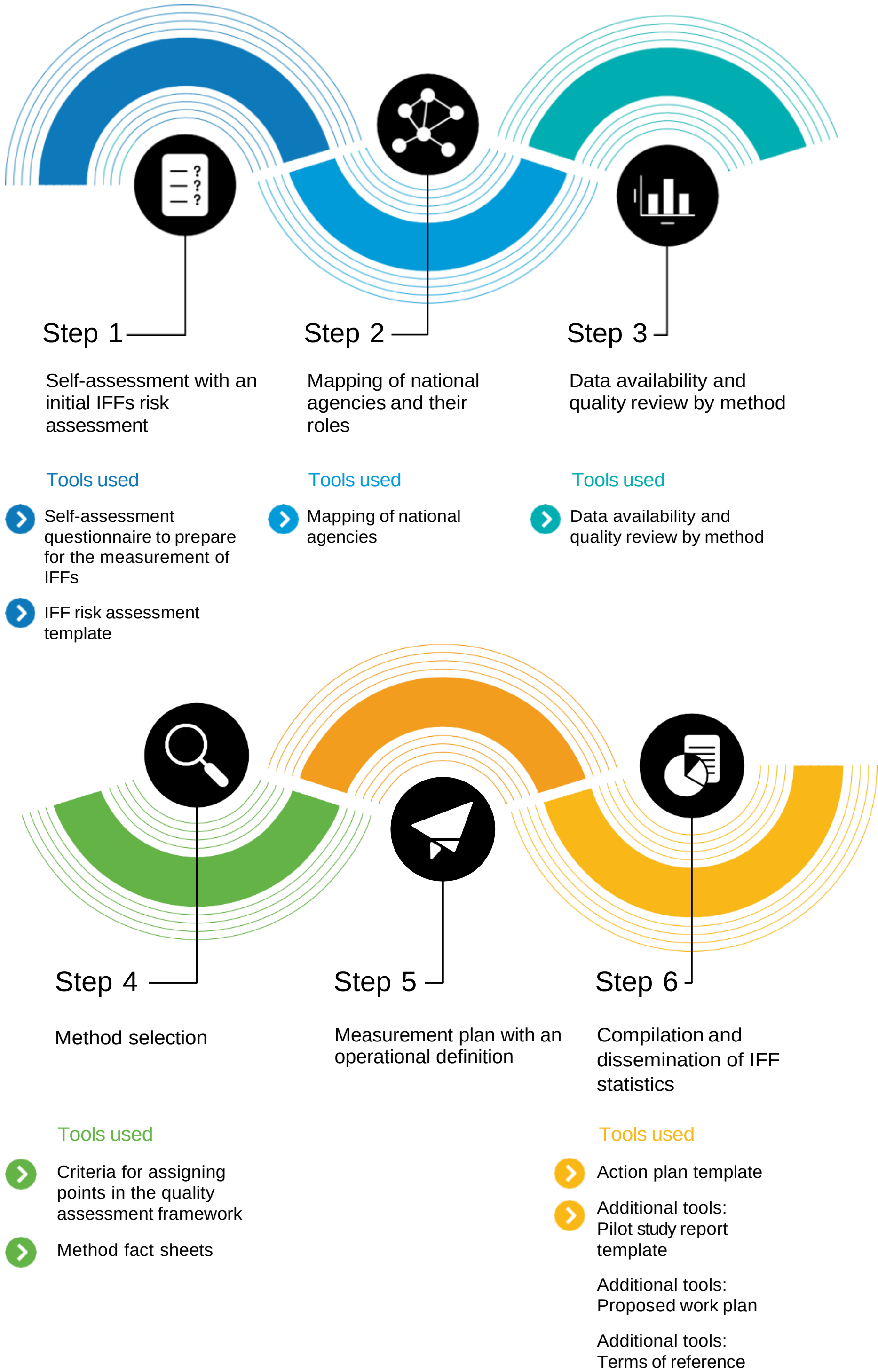
Methodological Guidelines (UNCTAD, 2021) proposed measurement techniques to measure tax and commercial IFFs, but also provided guidance to national authorities. These cover six steps to take to produce national IFF statistics, namely: initial IFF risk assessment and mapping of relevant national agencies to measure IFFs in a country, reviewing data availability and selecting appropriate methods, and ultimately conducting the measurement and compiling IFF statistics, including their dissemination (see Section 4).

At each of these steps, tools to support national authorities processing them, are devised within the Methodological Guidelines and available to interested stakeholders. These, outlined in Figure 6 as per the six steps, are:

- **Self-assessment questionnaire** serves to gather nationally relevant information on IFFs to comprehensively conduct IFF risk assessment and mapping of the national system of agencies.
- **IFF risk assessment** template provides areas to focus on when identifying IFF risks in a country. These cover: identification – environment for IFFs (such as formal and informal economy, financial system vulnerabilities, tax gap, trade flows), analysis – assessment of IFFs (categories and types of activities generating IFFs, enablers, likelihood and effects of IFFs), and evaluation – response to IFFs (governance, priorities for statistical work).

- **Mapping of national agencies** tool has been designed to help identify and map out various national agencies relevant for the compilation of IFF statistics, including their roles in the process.
- **Data availability and quality review** by method table has been designed to help evaluate data availability and quality. This includes an indicative list of variables for each method with the final selection depending on the national data environment. The elements in the evaluation include frequency, timeliness, access, coverage, granularity, interoperability/format (linking), fit for purpose, and availability.
- **Criteria for assigning points in the quality assessment framework** of methods elaborating on the criteria and pointing system within the assessment framework to assess each method with respect to soundness, source data, and results. It serves as a guiding tool to tier-classify methods.
- **Method fact sheets** which summarize the concept, strengths and limitations of the method, data requirements and other relevant information for specific method application.
- **Action plan** template sets steps for future measurement of IFFs in the country by identifying measures to improve the data infrastructure and statistical capacity of agencies, focusing on costs, time and impact of efforts needed, but also the division of work (lead and contributing agencies) as well at timeframe.
- **Pilot study report** template to support final report of pilot testing, covering the steps taken, but focusing on challenges, lessons learned and recommendations for future work.
- **Proposed work plan** identifies steps to be taken in the process and links them to more detailed activities, involved agencies, identifying start and end dates for the work.
- **Terms of reference for TWG** outlines the introduction, objective of the TWG, as well as planned activities and outputs, including the timetable for the overall work of TWG. Members are also listed.

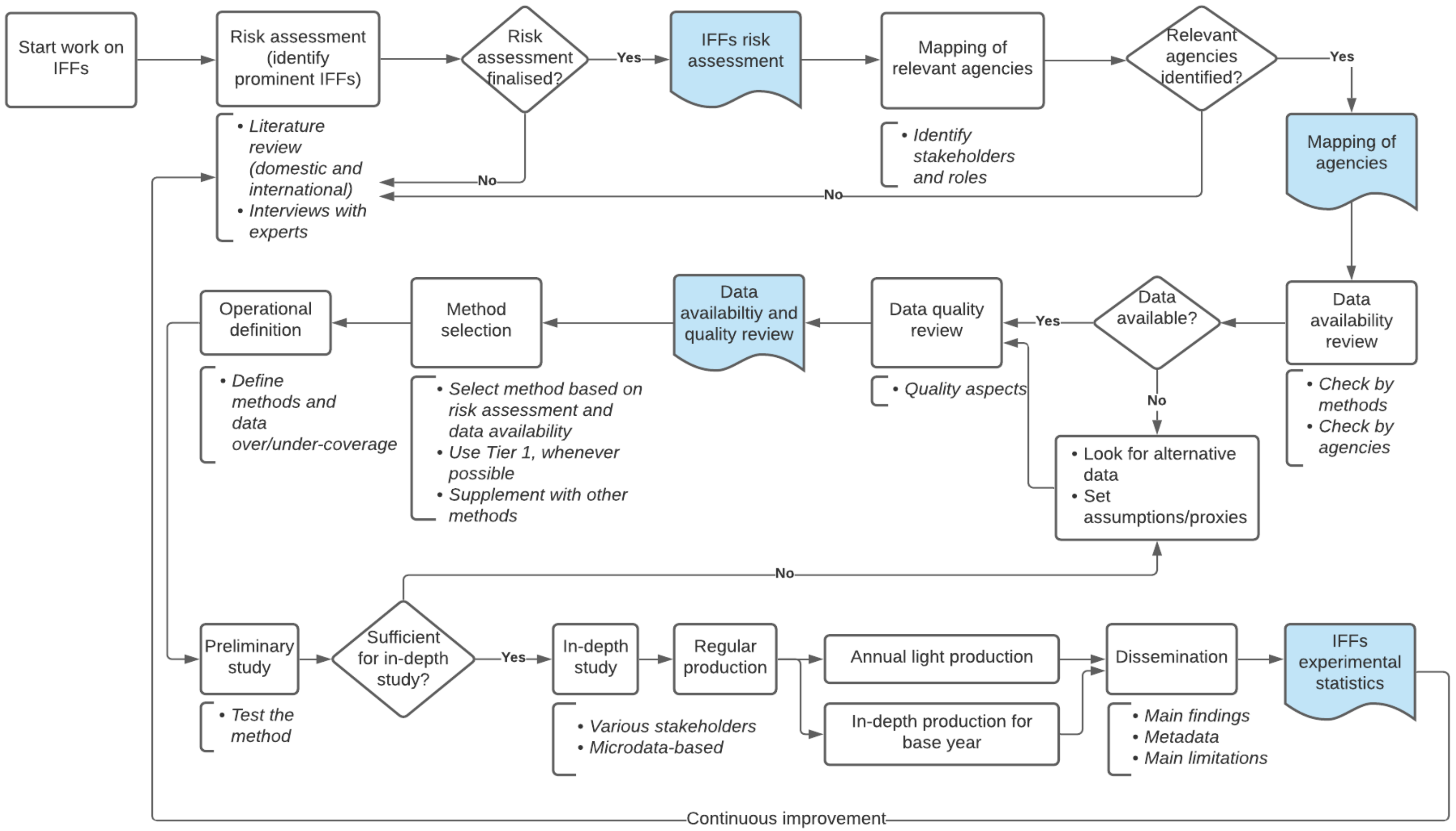
*Figure 6. Tools used in steps to measure illicit financial flows using Methodological Guidelines (UNCTAD, 2021)*




*Source: UNCTAD and ECA*

Schematic guidance through the process of measuring IFFs is depicted in a workflow to compile IFF statistics in Figure 7. Notable is the iterative nature of the measurement exercise, relying on additional information at each step, reinforcing the reliability of the entire process of compiling IFF statistics, starting with preliminary IFF studies and gradually implementing regular production of IFF statistics. The latter envisage also an in-depth production for base year, with years in between base years covered with annual, light(er) production. Continuous improvement is key in IFFs measurement.

*Figure 7. Workflow to compile illicit financial flows statistics*




*Source: (UNCTAD, 2021)*

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