UNCTAD ILLICIT TRADE FORUM

PRESENTATION ON

ILLICIT FINANCIAL FLOWS AND POLICIES FOR MONITORING: FOCUS ON THE EXTRACTIVE SECTOR.

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OUTLINE

- ILLICIT TRADE AND IFFS
- MAIN PRIORITIES AND CONCERNS
- CROSS-BORDER DIFFICULTIES
- EFFORTS HAVE BEEN MADE TO MEASURE ILLICIT TRADE AND RELATED IFFs
- MAIN STATISTICAL CHALLENGES IN DEVELOPING INDICATORS TO MONITOR IFFs
- POLICY ACTIONS HAVE BEEN TAKEN TO CURB DIFFERENT TYPES OF IFFs
- CASE STUDY (A MNE MINING COMPANY)
- CONCLUSION

Africa & Other Developing Countries

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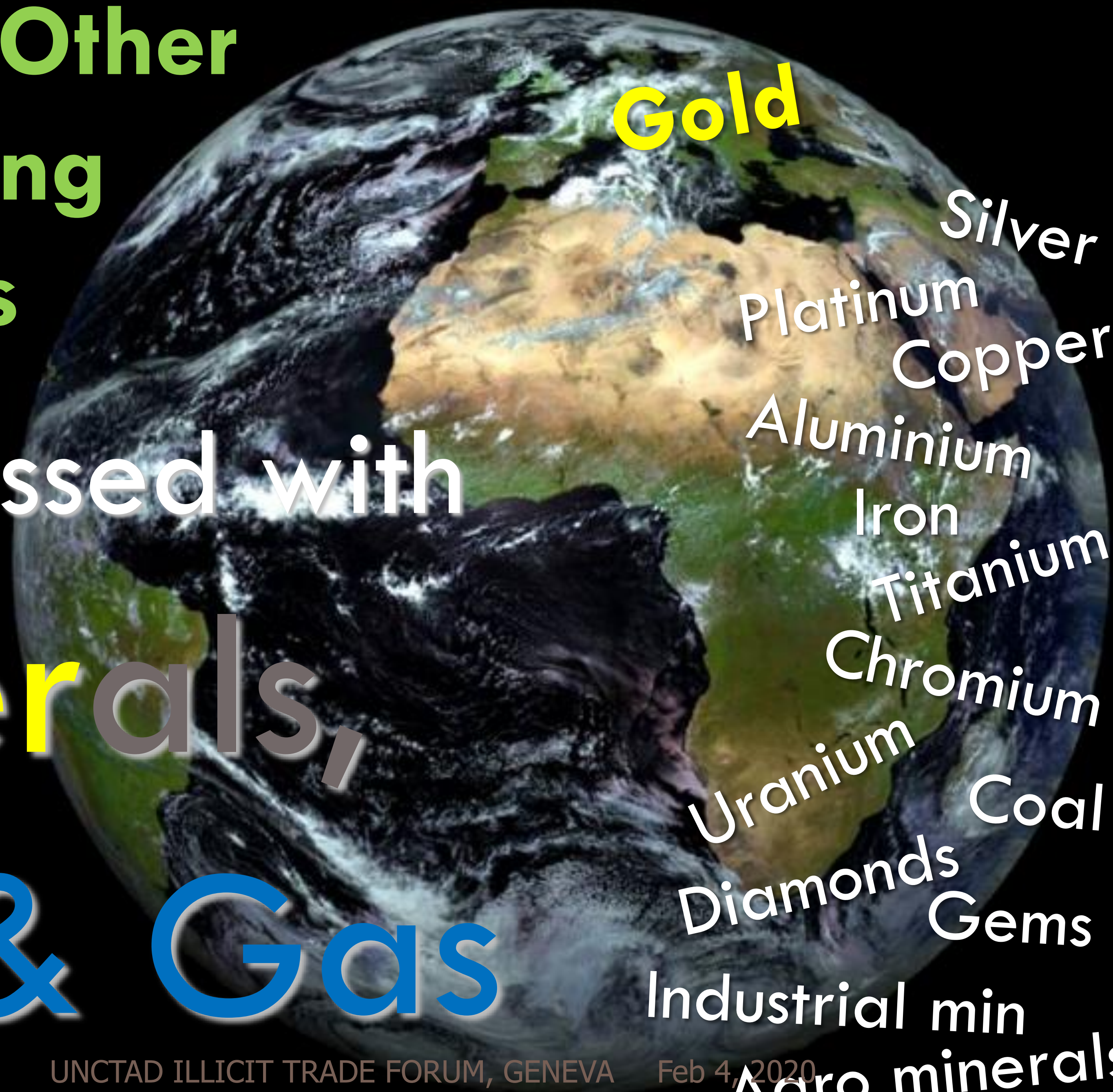
are blessed with

minerals,

Oil & Gas



But…

poor!!

ILLICIT TRADE AND IFFS

- *Illicit Trade including Trade mis-invoicing, including Customs fraud is one of the most damaging forms of IFFs since it poses massive threat to domestic revenue mobilization.*
- *Between 2000 and 2016, Africa for example lost about US 83 billion through trade mis-invoicing. Could close the infrastructure gap.*
- *It is therefore a type of IFF and could also be the channel where other types commercial, criminal or corrupt. A range of transfer practices, including mispricing, abusive tax prices, money laundering and bribery*
- *Do State institutions have the capacity to detect trade mis-invoicing ? Are national electronic customs systems where existent adequate ?*
- *Need to have Financial Intelligence Unit and equip them to act efficiently. Where legislations exist for trade mis-invoicing, customs fraud, smuggling etc, enforcement of these legislations is key*

PRIORITY AREAS & CONCERNS

- *Build robust institutions, excellent IT infrastructure to detect illicit trade, Pass Anti-Trade laws that would serve as a deterrent to those who engage in illicit trade.*
- *Sectors most affected include Trade, Extractive industries (mining, oil and gas), renewable natural resources ie Forestry and Fisheries. Foreigners involved*
  - *Illegal logging….**Rosewood**.. VPA-EU wood tracking system ineffective. Forest cover depleted.*
  - *Illegal Fishing, depletion of fishstock*
- *Actors include business men, junior and major mining companies, oil extraction and marketing companies, Forestry and Fisheries companies, Customs Officials, Politicians, Public and Civil Servants bureaucrats. Etc.*
- *Africa or Developing countries underdevelopment is largely due to IFF from all the sources as these monies could otherwise have been used for infrastructural development, eradicate health and disease, provide educational facilities etc.*
- *The institutions that are supposed to act to protect the state financial resources has virtually come to adopt IFF as a way of life as it has been practised over long periods of time and would not appreciate its harmful effects on the economy.*

CROSS BORDER DIFFICULTIES IN CURBING IFFs

- *Sharing of import and export information among states is a major difficulty that needs to be solved, it will be crucial in detecting variances in trade data.*
- *If one country has legislation or legal framework to promote co-operation in tax matters between revenue agencies of other countries, enforcement becomes an issue if the partner countries do not have such legal framework*
- *This is where Regional Economic Blocks such as ECOWAS, SADC can play a major role in ensuring trade information sharing on a sustained basis.*

STATISTICAL CHALLENGES IN DEVELOPING INDICATORS TO MONITOR IFFS

- *No globally-accepted methodology to monitor IFFs yet exists.*
- *UNCTAD and UNODC are custodians of the SDG indicator 16.4.1*
- *The lack of an agreed conceptual or methodological framework to measure IFFs hinders progress on understanding how large these flows are, where they originate from and what consequences they have.*
- *The absence of reliable, objective information undermines the ability to tackle the problems caused by IFFs.*
- *National policy makers face serious difficulties when national statistics reflect the global rearrangements of multinational enterprises rather than the domestic reality of people living in the country*
- *Statistics on national economies made reference to World Bank Reports sand similar Bretton Woods Institutions findings but not locally generated.*
- *Citizens of host nations give more credence to statistical data coming from the Bretton Woods Institutions than those coming from within*

STATISTICAL CHALLENGES IN DEVELOPING INDICATORS TO MONITOR IFFS

- *Understand illicit flows in the context of the legitimate national economy and how to avoid double-counting.*
- *"There can be double counting when we compare imports and exports of different countries, but also when we compare intermediate production and final consumption."*
- *Develop statistical definitions and typologies for the measurement of IFFs from a developmental perspective. (to cut across Anglophone and Francophone West Africa with UEMOA etc.*
- *Compilation of available data for different agencies, other existing data sources and exchange relevant experience in data collection across organisations.*
- *Methodologies to measure various types of IFFs and related phenomena to consider their feasibility for the measurement of the SDG indicator*
- *Methods to measure illegal economic activities and related money flows, aggressive tax planning, tax gaps, trade mis-invoicing, profit shifting, money laundering etc*

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

- *Entire value chain can be prone to IFF. it begins with* ***Licensing, Exploration, Development, Production, Transport & Storage and Marketing, Processing & Marketing, Abandonment and Decommissioning***
- *Minerals State Property, vested in President…. Some jurisdictions licenses granted by Presidency, (not by an autonomous body). Licensing First Come, First Served… not best option for economic rents… tendering is most often discouraged*
- *Minister has so much discretionary powers in the mining laws of most jurisdictions. Mining laws need to change to remove discretionary powers of Minister.*
- *The opaque nature of company ownership may encourage tax evasion and corruption. Disclosure of Beneficial Ownership must be a requirement.*
- *EITI focuses on disclosure for Mining, Oil and Gas but excludes Forestry, Fisheries etc.*

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

- *Deployment of an online system for Mineral Title Administration to reduce the incidence of corruption, human interface with the system.*
- *Establishment of an* ***Independent Gold or Mineral Assay Laboratory*** *is a must. Under-declaration of purity of gold for example, leads to illicit financial outflow.*
- *Guidelines need to be developed for CSR activities for MNEs operating in the Extractives to avoid over invoicing of cost social costs.*
- *Creation of a Multi-Agency Mineral Revenue Task Force to audit all corporate tax payments and Royalties (especially when it is a sliding scale regime).*
- *Develop Mine Fiscal Models for the extractive sector based in the country's fiscal regime.*
- *Data sharing with Revenue Authorities were mergers and acquisition occur in the mining sector……for capital gain tax payment …* Difficult when transactions are carried offshore.

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

- *Depreciation schedules in the mining Act of most countries on plant and machinery for mining usually have accelerated depreciation schedules.. usually written off within 5 years…..with excuse that investment need to the recovered quickly…*
- *Heavy equipment usually have useful lives from 15-20 years. They are written off in one one country, with zero book value,*
- *Possibility of refurbishing them and being sent to another country where the MNE operates. This will be treated as an initial cost of investment to be written off again….*
- *DECLARATION OF BENEFICIAL OWNERS AND DATA SHARING AMONG COUNTRIES WILL HELP ELIMINATE THIS*

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

- *In some jurisdictions, mining costs should be* ***wholly, exclusively and necessarily*** *incurred in the mining activity.*
  - *Some capital investments in the mining sector are completely unnecessary. Investment made just to create carry-forward losses into subsequent years to avoid payment income taxes…or lower taxable income.*
- *Dividend Payments depend on Dividend Policy of the MNE, and Host countries are at the mercy of the MNE. Without vigilance, dividends could be paid to shareholders outside host country without corresponding payment or lesser dividend payment to host countries*
  - *countries could go for a percentage of NET Cash Flow instead of relying on dividend policy of companies where they may not have representation on the Boards.*
- *Most MNEs operating in extractive sectors are registered in* ***Tax Havens !!!*** *What is the motivation for doing this ???... Revision in country laws may be required to deal with this…*

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

ARTISANAL AND SMALL SCALE MINING (RECENT MEASURES)

Before Regularization in 1987,… Cost of Gold smuggled out of Ghana was $30M annually. Due To environmental degradation..

- a total ban on small scale mining activities in Ghana irrespective of whether or not licensees had valid mineral licences .
- Collection from the Minerals Commission of all valid small scale licences issued by the Government for the purpose of vetting.
- Institution of Operation Vanguard aimed at stopping illegal mining
- Formation of “Galamstop”

- Water bodies have not recovered ….and degradation continues.. **Foreigners heavily Involved illegally in area of mining reserved by law for citizens.**
- Gold production from ASM almost doubled when the ban was in force. Where was the gold coming from ??. Declaration of gold with the Independent Assay Lab certification before gold exports has reduced illicit exports
- Gold from ASM is 40% (>1.6 M oz) of total gold production in Ghana.

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

- *Public interest and Accountability Committee (PIAC) to monitor the payments and use of oil and gas revenues. Does not cover mining sector* and not motivation to have PIAC extended to cover mining sector.
- *80% of mining royalties used by government as it pleases and 20% goes into a mineral development fund for distribution as specified in law. (Scope of PIAC being extended by initiative of GOGIC in drafting a bill "Extractive Industries Bill) for consideration of government.*

PETROLEUM AGREEMENTS AND MINING CONTRACTS

- **Negotiating bad, unconscionable mining and petroleum agreements** can be a major source of **legalizing illicit financial outflows from a Natural Resource Country.**

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

PETROLEUM AGREEMENTS

- *An oil company who acquired a block from another company under an agreement has sought and got approval for variation of the terms of that agreement with new clauses introduced after over a decade of the initial agreement being in force.*
- BASIS OF AMENDMENT
  - *Effect of new laws, regulations, changes in interpretation and practice of laws in the petroleum industry*
  - *Effects on petroleum operations caused by provisions in ITLOS*
  - *Transactions and operational changes in the Operator's organisation.*
- *Amended definitions include* ***Production Area and Development Area*** *all mean the same.*
- *"Operator" includes the contractor and persons appointed by the operator with approval of the Minister which approval shall not be unreasonably withheld.*

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

PETROLEUM AGREEMENTS

- *Minister of Energy to facilitate all other permits including environmental permits etc which shall be granted promptly..*
- *Exemption from VAT, Import duties, on plant and machinery and other fiscal imposts applicable under general law etc ousted to cover contractors and sub-contractors and other subsidiaries.*
- *Contractor and its sub-contractor to employ split-contract model of award of contracts and will not contribute towards local content fund which is provided for under the general law.*
- *Term of revised agreement is for 34 years….to be extended for 4 years to compensate for time lost by the contractor in commencing petroleum operations. Contractor reserves the right to extend the term based on its production profile and the Minister shall on the same terms extend the term of the lease.*

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

PETROLEUM AGREEMENTS

- *Right of pre-emption in the general law ousted under the new amendment.*
- *While the amendment ousted provisions of the Income Tax Act, 2015, Act 896, it considers unfavourable to it, it sought to maintain the provisions of a repealed Petroleum Income Tax Act, 1987 (PNDCL 188) under the Petroleum Agreement which it considers favourable to it.*

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
Stability Period	Indefinite (as long as mining leases are valid) and applies automatically to future leases	Limited to period specified by Law and to cover only existing leases	Any additional stability period must be earned with agreed investment with specified outcomes
Taxes and Duties	Exempt from duties and Taxes as long as leases remain valid except as provided herein in the IA	Subject to all duties and taxes except as exempted under general law or in the revised IA.	

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
Corporate Income Tax	Not to exceed 32.5% (listed 30%). Applicable to income from mining and other business activities including investment. Extensive Deduction for tax purposes	Fixed at 32.5% and applicable to income from mining only. Other businesses attract income tax under general law. Deductions fixed	The fixed corporate tax rate of 32.5% is applicable only to income derived from mining. This excludes hedge gains and other non-mining income, which will be taxed at the generally prevailing tax rate, *even during the stability period*.

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
Calculation of Corporate Tax	Elaborate and confusing. To cover entire life-of-mine	*For duration of stability period only*, taxable income calculated in accordance with law as at Jan 1, 2014. Thereafter, in accordance with generally applicable law	
Debt/Equity ratio	Ratio of 4:1	After short transition period, move to ratio of 2:1	Debt/Equity ratio now 3:1 under new Tax legislation (Act 896)

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
Capital gains	Capital gains taxable at 10% on basis set forth in Act 592	Capital Gains taxable under generally applicable law except for inter-company transfers of rights in which the MNE retains 25% or more	Capital gains tax regime extinguished by Act 896, so that gains on disposal of assets, including, mining assets, are taxed under general law as income and not as capital gains
Local taxes and duties	Not provided for in Agreement, so ***not payable and none ever paid***	MNE ***shall pay local and municipal taxes***, as paid by comparable bodies	This is new for the MNE

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
Withholding taxes on management fees	*Rate*: ***10%*** on fees paid for management to an affiliate ***or to a third party***	Rate: 10% on fees paid affiliates for management and technical services to; general rate ***(currently 20%) to third parties***	The 10% rate retained for payments to affiliates is the same as that in Double Taxation Agreements concluded by Ghana with 9 countries, with others awaiting signature.
Royalty	*Rate*: gold - ***3% fixed*** (3.6% in forest areas); other minerals – not to exceed 3%	Rate: gold - on ***sliding scale* of 3%-5% (3.6%-5.6%*** in forest areas)**;** other minerals – according to general law	

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
Duration of special regime	Exemptions to persist ***so long as any leases or renewals remained valid***	***After Stability Period***, exemptions end and the MNE subject to normal taxes, duties, etc.	
Forex	100% retention abroad of proceeds of gold sales and other receipts	MNE shall ***return to Ghana a minimum of 30% of its gross proceeds from the sale*** of gold to meet its obligations in Ghana for Taxes and Duties, wages, salaries and employee benefits and other payments for goods and services	

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
ADDITIONAL PAYMENTS (in relation to carried interest)	*No additional payment/signing–on premium*	NGGL shall make an **additional payment/signing-on premium***	Novelty in Ghana's Mining Regime. Paid on signing of the revised IA
BOARD MEMBERSHIP	***No right to nominate*** member to NGGL Board Of Directors	The Government shall have the ***right to nominate*** one member of MNE Board	

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
GOVERNING LAW	*Terms of the agreement* ***prevail over conflicting laws of Ghana and applicable international law***	***Removed***	
MOST FAVORED TREATMENT	In the event Govt. permits ***more favorable treatment*** to other persons, ***same must be extended to the MNE***	***Removed***	

POLICY ACTIONS TO CURB DIFFERENT TYPES OF IFFS: FOCUS ON EXTRACTIVES

MINING INVESTMENT AGREEMENT - A CASE STUDY

PARAMETER	ORIGINAL IA	REVISED IA	REMARKS
ADDITIONAL MINING LEASES	Terms of IA extend to automatically to ***all future mining leases granted MNE anywhere***	IA now restricted to ***leases of areas adjoining existing Production Areas***	Removes excessive concession of agreed terms applying automatically to ***any*** lease granted MNE ***anywhere*** in Ghana. Now limited to natural extensions from existing lease due to geological formation, as is the general position in the law

SOME MEASURES IN COMBATING IFFs

- NATIONAL STRATEGY…
  - *legal and law enforcement, Resource Allocation*
- LEGAL FRAMEWORK…
  - *Criminalization of IFFs , Dedicated legal entities*
- ADMINISTRATIVE PROCEDURES..
  - *Money Laundering, Suspicious Transactions etc*
- SPECIAL FOCUS AREAS
  - *Politically Exposed Persons,*
- REGIONAL AND INTERNATIONAL CO-OPERATION
  - **Multilaterial and Bilateral Agreements, Regional Economic Blocks etc**

CONCLUSION

ILLICIT TRADE AND ILLICIT FINANCIAL FLOWS ARE THE BIGGEST THREAT TO THE ACHIEVEMENT OF TARGETS UNDER THE SDGs.

IF PRAGMATIC STEPS ARE NOT TAKEN TO DEAL WITH THEM, ATTAINMENT OF SDG GOALS BY 2030 MAY BE A MIRAGE.

Questions | Comments | Contributions