Chapter 6

Domestic resource mobilization and financing for the Sustainable Development Goals

One of the main motivations for tackling IFFs originates in concerns about the capacity of countries in Africa to raise sufficient revenue to invest in achieving the Sustainable Development Goals (Goal 17). This highlights the importance of increasing tax revenue, to help curb IFFs and recover stolen assets. The direct impact of IFFs on social development is mainly channelled through lower levels of domestic resource mobilization, which adversely affect capacity in Africa to finance the achievement of the Goals.
CURBING CAPITAL FLIGHT could contribute almost 50% of the investment needed for climate change adaptation and mitigation in Africa.

PER PERSON, COUNTRIES WITH HIGH IFFs spend:

- 75% on health
- 42% on education

compared to countries with low IFFs.
This chapter highlights some of the detrimental impacts of IFFs on social development and aims to provide a better understanding of the potential opportunity costs due to IFFs with regard to public finance and social expenditure in countries in Africa (Moore, 2012; Herkenrath, 2014; Carbonnier and de Cadena, 2015). Section 6.1 focuses on recent domestic resource mobilization. Sections 6.2 and 6.3 provide an assessment of Goals-related outcomes and how capital flight relates to the financing gap impeding the achievement of the Goals in Africa. The analysis is complemented by a discussion in section 6.4 on climate change-related financing needs in countries in Africa. Section 6.5 highlights the potential for multilateral cooperation in curbing IFFs and a case study of taxation in the gold mining industry. Section 6.6 provides a case study from Nigeria and discusses country-specific instruments for tackling IFFs. Section 6.7 summarizes the key points.

6.1 Illicit financial flows and Government revenue in Africa

The state of Government revenue
Governments in Africa raise taxes equivalent to 16 per cent of GDP, a figure that has been increasing steadily since 2010. Although the recent trend is upward, this increase largely reverses a decline that took place in the 1980s and 1990s, as structural adjustment reforms significantly reduced tax revenue from international trade. ODA and revenue from a boom in natural resources mitigated the reduction in tax revenue during this period. If natural resource revenue is included, countries in Africa raise taxes amounting to 18 per cent of GDP. Income generated only from resources (tax and non-tax) amounts to 10 per cent of GDP, on average, in countries in Africa (figure 17). As revenue from taxes on international trade has declined, there has been a broadening of the revenue base. Personal income tax and, significantly, value-added tax have both become more important sources of revenue in Africa, enough to offset the decline due to lower tariff revenue. Personal income tax has nonetheless doubled as a share of GDP in countries in Africa in the past two decades. According to data from ICTD and UNU-WIDER, corporate income tax amounts to around 3 per cent of GDP in nearly all countries of the world, including countries in Africa.
Figure 17
Main sources of Government revenue in Africa
(Percentage of gross domestic product)

Source: UNCTAD calculations based on the ICTD and UNU-WIDER government revenue database and the World Bank world development indicators.

Countries in Africa, as do other developing countries, raise less total revenue than developed countries (33 per cent of GDP). The only taxes with regard to which countries in Africa raise more as a share of GDP than OECD member countries are those related to international trade. The large share of the informal sector and the number of small-scale firms limit the ability to raise a large amount of taxes. In addition, a taxation system that favours MNEs that exploit natural resources and pay taxes in the countries in which their headquarters are located narrows the tax base, in particular in resource-dependent countries (UNCTAD, 2019a; chapter 3).

Tax revenue and illicit financial flows
Revenue losses from corporate tax avoidance are significant. Developing countries lose a greater share of their tax revenue in this way than do developed countries, yet their performance in raising corporate tax, measured as a share of GDP, is already similar to that of developed countries (Hearson, forthcoming). The level of corporate tax raised may
be expected to increase because statutory corporate tax rates in developing countries tend to be higher yet, by contrast, effective rates may be lower than the statutory tax rates as a result of tax incentives. However, the diversity of the tax base in developing countries suggests that dramatically increasing the overall revenue raised will require efforts across a range of sources including, but not limited to, corporate income tax.

The magnitude of overall capital flight and estimated tax avoidance is compared by region in figure 18. Revenue loss from tax avoidance is on average highest in Middle Africa, Northern Africa and Eastern Africa (2.7 per cent of GDP), compared with Southern Africa (nearly 2 per cent of GDP) and Western Africa (2.3 per cent of GDP). Estimates of high levels of capital flight, ranging from a median of 10.3 per cent in Western Africa to 2.7 per cent in Northern Africa, are also associated with lower levels of domestic revenue. Some of the key challenges in increasing tax revenue relate to compliance with laws and administrative capacity to collect taxes. Across countries, there are large tax-related gaps, namely, the difference between potential and actual value-added tax, ranging from 92 per cent in the Central African Republic to 13 per cent in South Africa (UNECA, 2019). These gaps may arise due to the prevalence of special provisions or exemptions for value-added tax laws or limitations in administering the collection of value-added tax, including issues related to inefficiency, limited capacity, fraud and unreliable consumption data. Coulibaly and Gandhi (2018) estimate that improving tax efficiency and closing the average tax-related gap of 20 per cent could raise tax revenue by 3.9 per cent of GDP. Improving governance through the better control of corruption and effective enforcement of existing laws could largely reduce inefficiencies and could help raise an additional $110 billion per year. Total capital flight amounted to roughly $88.6 billion per year on average in 2013–2015.
Figure 18
Capital flight and revenue loss from tax avoidance, median by region, 2013–2015
(Percentage of gross domestic product)

Source: UNCTAD calculations based on Cobham and Janský (2018) and Political Economy Research Institute database.

Note: Negative values are deleted; not all countries have data on capital flight and averages are therefore biased towards countries for which there is data available and high levels of capital flight; average values of capital flight as a percentage of GDP in 2013–2015 are 3.0 (Northern Africa), 5.9 (Southern Africa), 9.2 (Eastern Africa), 12.9 (Middle Africa) and 34.9 (Western Africa).

6.2 How illicit financial flows impair Goals-related outcomes

Efforts to increase domestic resource mobilization are crucial in achieving the Goals but are not a panacea. At the same time, it is equally important to increase the efficiency of spending on Goals-related outcomes. This section considers both with regard to estimates of capital flight and expenditure, in relation to current estimates of Goals-related financing needs. The estimates do not imply causality and are driven by national characteristics that affect both macroeconomic performance and institutional quality. Countries with high levels of IFFs spend 75 per cent of the amount that countries with relatively low levels of IFFs spend on per capita expenditure on health and, with regard to education, 42 per cent (figure 19). Restraints on higher levels of public spending are also determined by the overall composition of Government expenditure. According to the IMF government
finance statistics, fragile States in particular may have higher levels of expenditure on
defence and general public services, which includes debt service. In 2015, countries in
Africa spent, on average, $354 per capita on Goals-related outcomes, compared with a
global average of around $3,000 per capita (Kharas and McArthur, 2019).

Figure 19

Africa: Total health and education expenditure, median by level of capital flight
(Dollars per capita)

Source: UNCTAD calculations based on World Bank world development indicators.
Note: For the classification of low and high levels of capital flight, see table 8.

Can lower levels of expenditure be directly associated with inferior outcomes in health
and education? In order to project what re-investing IFFs into social development could
mean, the analysis uses available data on the under-5 mortality rate, current expenditure
on health as a share of total Government expenditure and an estimated health-outcome
elasticity of increases in public expenditure of -0.19 and -0.09 in countries in Africa from
Makuta and O’Hare (2015). Achieving target 3.2, aimed at reducing under-5 mortality
to at least as low as 25 per 1,000 live births, is strongly linked to other health indicators
such as malnourishment. The best data coverage is also available for this variable.

In 2018, the under-5 mortality rate in countries with relatively high levels of capital flight
was, on average, 59, down from 66 in 2015 (figure 20). Countries with lower levels of
capital flight relative to GDP had the slightly lower rate of 55, down from 61 in 2015.
Assuming an ambitious scenario in which the health sector is prioritized and curbed capital

flight leads to increases in health expenditure as a share of GDP by the same amount, countries with high levels of capital flight could reduce the mortality rate to 20 and achieve target 3.2. In a more realistic scenario in which the share of health expenditure in total expenditure is kept constant at 6 per cent of Government revenue, there may be limited improvement through tackling capital flight and, due to low elasticities of health outcomes from spending increases, curbing capital flight would have only a marginal impact on reducing the mortality rate (Grigoli, 2015; Moulemvo, 2016; Manuel et al., 2018; Kharas and McArthur, 2019). Countries in Africa can come closer to achieving target 3.2 only if all curbed capital flight is devoted to health expenditure. For example, in the Congo, while social expenditure would largely increase from investing capital flight into the local economy, “it would enable only a marginal effect on the primary school competition rate [and] on the mortality rate of children below one year of age” (Moulemvo, 2016:121). A country-level comparison suggests that countries in Northern Africa and Southern Africa are on track to achieve target 3.2 and that Middle Africa and Western Africa are not.

Figure 20
Projections on achieving target 3.2, by level of capital flight and region
(Under-5 mortality per 1,000 live births)

Source: UNCTAD calculations based on World Bank world development indicators.
Note: Average values of capital flight as a percentage of GDP in 2013–2015 are 3.0 (Northern Africa), 5.9 (Southern Africa), 9.2 (Eastern Africa), 12.9 (Middle Africa) and 34.9 (Western Africa); for the classification of low and high levels of capital flight, see table 8.
Compared with health-related outcomes, differences in education outcomes are less pronounced with regard to estimates of capital flight, which can be related to greater opportunity costs and the personal transaction costs of attending school (figure 21). Higher levels of investment in education and an improved quality of education benefit productivity through the acquisition of knowledge. In the analysis, the rate of enrolment in primary education serves as the proxy for educational performance, as the best data coverage over time and across countries is available for this variable. The possibility of acquiring an education strongly depends on household income levels and microeconomic factors not related to macroeconomic measures of capital flight. Higher levels of Government spending could, however, not only finance more teachers and schools but also provide for better infrastructure to allow for greater access to educational facilities.

**Figure 21**

**Africa: Primary net enrolment rate, by level of capital flight**

(Percentage of age group)

![Graph showing primary net enrolment rate by level of capital flight for girls and boys in Africa.](image)

Source: UNCTAD calculations based on UNESCO Institute for Statistics data and World Bank world development indicators.

Note: UNESCO defines the net primary enrolment rate as the total number of students in the theoretical age group for a given level of education enrolled in that level, expressed as a percentage of the total population in that age group; for the classification of low and high levels of capital flight, see table 8.
Grigoli (2015) and Ihugba et al. (2019) note that increased expenditure on education is inefficiently deployed in many countries in Africa. Such inefficiencies tend to be more pronounced in countries with a large rural population and point to difficulties in accessing education due to poor rural infrastructure, high income inequalities and inefficient institutions. Lower levels of capital flight positively impact productivity levels and income generation and thereby lead to multiple opportunities to boost private and public investment in education. Public investment in early childhood education can also have positive impacts on productivity and gender equality because women as primary caregivers can spend more time engaging in higher paid work (Alfers, 2016). Gender equality in education can also spur productivity growth and structural transformation and at higher levels improves institutional quality and, inter alia, potentially contributes to reducing IFFs (Klasen, 2002; Klasen and Lamanna, 2009; Trenczek, 2016).

6.3 Curbing illicit financial flows can help finance the achievement of the Goals

The comparison of levels of IFFs with Goals-related financing needs is based on Kharas and McArthur (2019), in which the multiplier effects of various dimensions – agriculture and rural development, health, education, social spending, infrastructure, biodiversity and justice – are considered and it is noted that none of the Goals can be treated in isolation. In order to estimate country-specific Goals-related financing needs, Kharas and McArthur (2019) build on existing literature for 10 different related sectors (UNCTAD, 2014b; UNESCO, 2015; Stenberg et al., 2017; Manuel et al., 2018) and the estimation of Goals-related spending in 2025 considers each country’s spending level as a share of GDP in 2015 and applies a 1.13 multiplier relative to each country’s forecasted growth in GDP per capita until 2025. In estimating financing needs in 2025, Kharas and McArthur (2019) acknowledge that higher levels of Goals-related spending do not guarantee greater outcomes. Inefficiencies due to poor access to health and education facilities and a lack of quality infrastructure can be addressed when public spending is distributed across various dimensions of the Goals. Therefore, using the term “needs gap” instead of “financing

Tackling illicit financial flows for sustainable development in Africa

Kharas and McArthur (2019) emphasize that there is not only a lack of finance but also a lack of efficiency. Section 6.2 addresses this aspect in the discussion of low efficiency in social expenditure for increasing health and education outcomes (for further empirical evidence of low spending efficiency in Africa, using cross-country estimates, see Grigoli and Kapsoli, 2013; Gaspar et al., 2019).

The estimate of the financing gap by region is compared with per capita estimates of capital flight (figure 22; estimates are displayed for illustrative purposes and should not be taken as exact numbers). The estimated Goals-related financing needs are greatest in Middle Africa ($289 per capita) and Western Africa ($274 per capita). In the Middle Africa region, the needs gap is highest in the Central African Republic and the Congo. Curbing the high level of capital flight across countries in Africa, estimated at $78 per capita, could close the financing gap by 33 per cent. In Southern Africa and Western Africa, in which the estimated capital flight relative to the population is greatest ($159 and $107 per capita, respectively), curbing capital flight could reduce the estimated Goals-related financing gap by 75 and 40 per cent, respectively.

Figure 22
Total financing gap and capital flight, by region, 2013–2015
(Dollars per capita)

Source: UNCTAD calculations based on Kharas and McArthur (2019) and Political Economy Research Institute database.
Note: Regional estimates are derived from the sum of the Goals-related financing gap per region, divided by total regional population; only positive estimates are included.
The needs gap differs between countries even with similar per capita GDP and is subject to uncertainties due to data limitations. Significant differences arise from differences in income distribution, the local disease burden, soil suitability for agriculture, exposure to droughts and floods, migration patterns and ease of access to trading partners, among others (Kharas and McArthur, 2019). Country-specific estimates of Goals-related financing needs are required to yield a better understanding of the challenges and financial possibilities in each country. In some countries, the Goals have been directly integrated into national development plans, aimed at providing estimates on sectoral needs. For example, in Rwanda, the Goals and targets have been integrated into the National Strategy for Transformation 2017–2024 and sectoral initiatives have been implemented to estimate sectoral needs for achieving the strategy.

This section considers estimates of Goals-related spending by the public sector, yet the private sector also has a key role, as it both generates and can help ameliorate the negative effects of IFFs. Some MNEs have initiatives within value chains for investing in local human capital accumulation in health and education, as well as in infrastructure, to boost firm-level productivity.

### 6.4 Special case of climate change-related financing needs and illicit financial flows

Many developing countries, including countries in Africa, are highly vulnerable to the effects of climate change, which has been associated with a higher incidence of natural disasters. Occurrences of natural disasters and the associated costs have significantly increased since 2005 (figure 23). Such trends place a heavy burden on sustainable development in Africa. Total reported costs amounted to $796 million in 2018 and rose to $2.4 billion in 2019. Such costs do not include the long-term costs of lower levels of productivity. There is a significant negative effect from natural disasters on labour productivity in Africa (chapter 5). The mobilization of significant financial resources is required in each country to adapt to climate change.
Figure 23
Africa: Number of natural disasters and related costs
(Millions of dollars)

Note: Total estimated damages are calculated as a value of all damage and economic losses directly or indirectly related to each disaster; natural disasters (occurrences and costs per year) include all subgroups (climatological, geophysical, biological, hydrological and meteorological).

Measuring the level of financing needed to achieve the goals of the Paris Agreement is challenging. Kharas and McArthur (2019) refer to levels of required Government spending with regard to biodiversity conversation, which relates to environmental protection expenditure but does not include the costs of climate change mitigation and adaptation. In order to assess the magnitude of capital flight in relation to financing needs with regard to climate change mitigation and adaptation, two estimates are compared, namely, investment needs for climate change mitigation and adaptation; and capital flight.

Investment needs for climate change mitigation and adaptation are based on intended nationally determined contributions under the Paris Agreement that have been submitted by all parties except Libya, although commitments vary widely with regard to details of the sectors targeted, whether commitments are conditional based on financial needs and whether financial needs have been quantified. With regard to sectoral coverage, 38 countries include commitments with regard to climate change mitigation or adaptation in agriculture and two countries, the Congo and Guinea, in mining (for a discussion of nationally determined contributions, see UNCTAD, 2019a). Financial needs in developing
countries are rarely quantified at the country level, mainly due to uncertainties and difficulty in estimating the impact of climate change. For example, UNEP (2016) estimates that adaptation costs will be between $280 billion and $500 billion per year by 2050 and mitigation costs will be between $140 billion and $175 billion. Shimizu and Rocamora (2016) state that, to achieve climate change mitigation and adaptation by 2030, financing needs in sub-Saharan Africa are $2,457 billion or, on average, $60 billion per country, as well as an estimated $71 billion per country in North Africa and the Middle East, for a total of $356 billion. In sub-Saharan Africa, to meet the costs of climate change mitigation and adaptation by 2030, an estimated $153.5 billion needs to be mobilized each year. In per capita terms, this is around $152 per year until 2030 (country-specific estimates are not possible due to a lack of data and per capita estimates are only for comparative purposes and should not be interpreted as a population weighted estimate of financing needs). A comparison of estimated climate change-related financing needs with total annual capital flight in sub-Saharan Africa suggests that curbing capital flight could contribute almost 50 per cent to the total climate change mitigation and adaptation needs of countries in sub-Saharan Africa (figure 24).

**Figure 24**

**Sub-Saharan Africa: Annual climate change-related finance needs by 2030 and capital flight**

(Millions of dollars)

![Chart showing annual climate change-related finance needs by 2030 and capital flight](chart.png)

**Source:** UNCTAD calculations based on Shimizu and Rocamora (2016).

**Note:** The estimated financing needs of $2,457 billion in sub-Saharan Africa until 2030 are divided by 16 (2015–2030) to allow for a comparison with total annual capital flight.
6.5 Initiatives to promote domestic resource mobilization and tackle illicit financial flows

**Multilateral cooperation for resource mobilization: Reclaiming stolen assets**

Following the adoption by the General Assembly of resolution 58/4 and the United Nations Convention against Corruption in 2003, StAR was launched in 2007 as a joint project of UNODC and the World Bank (Ajayi and Ndikumana, 2014). Article 53(b) of the United Nations Convention against Corruption states that each State Party shall, in accordance with its domestic law, “take such measures as may be necessary to permit its courts to order those who have committed offences established in accordance with this Convention to pay compensation or damages to another State Party that has been harmed by such offences”. Stolen assets are the proceeds of corruption and countries in Africa face significant legal and practical constraints in dealing with stolen assets and reclaiming them. Through StAR, a total of $1.53 billion has been recovered and returned to countries in Africa, but this amount is not significant, compared with the high level of capital flight.

Through the StAR initiative, African countries have recovered $1.5 billion equivalent to only 0.5% of capital flight.

As at January 2020, the database of the initiative reported 79 claims, yet only 17 countries had an ongoing or complete case; 22 cases have been completed but only 10 of these have resulted in stolen assets being reclaimed. The most active jurisdiction of asset recovery is Switzerland, followed by the United Kingdom and the United States. With regard to the number of cases and success with regard to recovered assets, at up to $1.48 billion in total, Nigeria is the most active country (figure 25).
**Figure 25**

Returned stolen assets, by country

(Sum in dollars)

![Figure 25: Returned stolen assets, by country](image)

*Source: UNCTAD calculations based on the database of StAR.*

The database of StAR also shows the length of time required for proceedings; many cases opened before 2010 are still ongoing. In addition, the amount of assets returned are less than the assets that were frozen, indicating the level of difficulty in reclaiming stolen assets (Gray et al., 2014). This is closely related to the difficult process of gathering information and converting it into actionable evidence. The case that has seen the greatest amount reclaimed, namely, $723 million from Switzerland to Nigeria, provides an example of how returned assets can be used in sustainable development, as the agreement states that projects in the sectors of health, education, water, electricity and roads should be funded, with the World Bank responsible for monitoring.  

It is necessary to undertake multilateral efforts to strengthen asset recovery policies, standards and actions. StAR is the leading institution in the global network of initiatives, which include the Asset Recovery Inter-Agency Network for Southern Africa, founded in 2009; the Asset Recovery Inter-Agency Network for East Africa, founded in 2013; and the Asset Recovery Inter-Agency Network for Central Africa, founded in 2016.

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and the Asset Recovery Inter-Agency Network for West Africa, founded in 2014. The secretariat of the Camden Asset Recovery Inter-Agency Network and the European Union Agency for Law Enforcement Cooperation organize annual meetings for training, exchanging knowledge and sharing information (for further information on other regional networks and the Global Focal Point Network on Asset Recovery, see StAR, 2019). Current projects to tackle IFFs show how greater cooperation in capacity-building can facilitate stolen asset recovery. For example, as part of a German Corporation for International Cooperation project, multi-agency teams were established to conduct financial investigations in Kenya and, in 2016–2017, the national Ethics and Anti-Corruption Commission was able to increase its conviction rate by over 50 per cent and recovered a total of $27 million in stolen assets in the first four months of 2019 alone.\textsuperscript{73} This approach has been promoted within the Asset Recovery Inter-Agency Network for East Africa.

\textbf{The need for more effective tax regimes: Taxation in the gold mining industry}

As noted, most trade-related IFFs originate in extractive industries, in which rents are created from the exploitation and export of non-renewable resources that constitute national assets, and the extractive sector is typically dominated by MNEs. This section discusses in more detail effective tax regimes for extractive industries to estimate the share of rents that should be collected by Governments, building on the discussion of tax regulatory frameworks and domestic legislation for extractive industries (chapter 4). This section uses data from a database developed by the Fondation pour les Études et Recherches sur le Développement to highlight the special case of taxation in the gold mining industry in Africa, which allows for an evaluation of revenue losses from unequal taxation resulting from exemptions, with data for 21 countries.\textsuperscript{74} The database combines all of the juridical sources from the selected countries, to provide the legal framework for tax regimes applicable to gold mining companies, including mining codes, implementation decrees, tax laws, annual finance laws and other fiscal laws. This permits the calculation of the share of rents that should theoretically go to the State, using a cash flow model developed by the IMF. The average effective tax rate is simulated for different representative mining projects, depending on the grade of a mine and the gold selling price. The mining tax rate may decrease with the grade of a mine, which indicates that there is a regressive tax rate applied to companies when a mining project is more profitable (Laporte et al., 2017). In 2018, countries

\textsuperscript{73} See https://www.giz.de/en/worldwide/39748.html.

\textsuperscript{74} Benin, Burkina Faso, Chad, Congo, Côte d’Ivoire, Cameroon, Democratic Republic of the Congo, Gabon, Ghana, Guinea, Kenya, Madagascar, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone, South Africa, United Republic of Tanzania, Zimbabwe.
with the most regressive tax schemes for high-grade mines included Gabon, Mali, the Niger, Nigeria and Zimbabwe. A regressive tax scheme tends to increase inequalities when companies with low levels of profitability pay higher taxes and are less able to allocate an appropriate amount to economic savings and investments, worsening the economic situation (UNECA, 2019). Widespread tax evasion not only exacerbates the challenge faced by tax authorities in Africa in providing basic public services, but also limits efforts to address urgent institutional reforms (Prichard and Bentum, 2009; Herkenrath, 2014; chapter 4). Kharas and McArthur (2019) state that greater royalties from mineral taxation would potentially reduce profit shifting and IFFs, but such tax benefits might still be low in terms of scale. In contrast, corporate income taxes that are higher in terms of scale could also have negative effects on tax revenue due to incentive diversion.

Figure 26 shows the composition of the average effective tax rate and the relative importance of different tax elements based on legal origins. The elements include profit-based taxes such as dividend and interest tax (a withholding tax), corporate income tax (an income tax on the profits of companies) and resource rent tax (a direct tax on net cash flow that is rarely applied due to the difficulty of administration); free State equity (shareholding); and production-based taxes such as mining royalty (an ad valorem tax on the value of the ore when it is sold or exported) and fixed and ground fees (usually related to the surface and/or property of a mine). The most common profit-based instrument is corporate income tax and almost all production-based instruments involve mining royalties (Laporte et al., 2017; Bouterige et al., 2019). Since 2002, French-speaking countries have tended to rely more on mining royalties and free State equity than corporate income tax (Bouterige et al., 2019). The definition of mining royalties varies across countries and this may also result in different tax rates, which can be fixed, variable or progressive; most countries apply a fixed rate (Laporte et al., 2017). In contrast, English-speaking countries remain reliant on corporate income tax, with almost no use of free State equity until 2017.
Figure 26
Africa: Composition of average effective tax rates
(Share of total average effective tax rate)

(a) English-speaking countries

(b) French-speaking countries

Source: UNCTAD calculations based on the Fondation pour les Études et Recherches sur le Développement database

Note: The average effective tax rate shown is that for high-grade mines and a gold selling price of $1,400 per ounce.
The use of corporate income tax has been declining, indicating that profit-based taxes have been less utilized, which could be a missed opportunity if the demand for gold increases. Corporate income tax is sometimes accompanied by a minimum tax to provide a floor for State revenue, mostly in French-speaking countries (the minimum tax applies to turnover and ranged between 0.5 and 2.5 per cent in 2018; Bouterige et al., 2019). Applied corporate income taxes range from 20 to 35 per cent in the 21 countries included in the database. Moreover, a tax on mineral resource rents could be a neutral tax, yet clearly defining the tax base has been a challenge (Bouterige et al., 2019). Based on the data, in 2018, countries using mining royalties the most as a share of all instruments (with levels above 20 per cent) were the Niger, Zimbabwe, Mali, Mauritania and Senegal. With the exception of Zimbabwe, these are French-speaking countries in Western Africa. However, some countries, although they are also French-speaking countries, have had the lowest shares (less than 10 per cent) of mining royalties, such as Benin, Chad and Madagascar.

In 2016–2018, the average effective tax rate remained relatively stable in most countries, but decreased in Cameroon and increased in Chad, the Democratic Republic of the Congo, Kenya, Senegal, South Africa and the United Republic of Tanzania. The increases in some of these countries can be attributed to the implementation of different tax rates. For example, the Democratic Republic of the Congo, Senegal, Sierra Leone and the United Republic of Tanzania increased mining royalties and Chad, the Democratic Republic of the Congo and Sierra Leone introduced a tax on mineral resource rents. The use of free State equity has also increased, to allow States increased access to information and to receive direct dividends. Among the countries with the greatest increases in average effective tax rates, mining acts have been implemented in Chad, the Democratic Republic of the Congo, Kenya, Senegal and the United Republic of Tanzania.

With the establishment of AfCFTA, the complexities of mining tax schemes and their treatment are of importance for many Governments in Africa. Greater continental efforts through national implementation of AMV are required, to address the complexity of different aspects of taxing extractive industries and how tax reforms and mining contracts may be improved in order to increase the average effective tax rate and boost Government revenue from natural resources (chapter 3). The selection of profit-based or production-based instruments also remains a complex issue, which requires further research beyond the scope of this report. The public finances of States are likely more affected by the business cycle if tax schemes are less regressive. To maximize commodity revenues for the financing of sustainable development, Governments could
use profit-based instruments such as corporate income tax during periods of sustained economic expansion. When commodity prices are high, using profit-based instruments is beneficial to Governments because they can capture a greater share of the financial gain. However, when commodity prices are low, it may be better for Governments to use production-based instruments such as mining royalties. The taxation of profits, particularly in extractive industries, has the disadvantage that the tax base can be manipulated in numerous ways. Therefore, Governments could consider, for example, shifting to taxation methods that are easier to administer.

6.6 Policy instruments to tackle illicit financial flows: Case study from Nigeria

Nigeria has the largest economy in Africa and is the main oil producer. The experience of Nigeria presents an interesting case study of how tackling IFFs can improve domestic resource mobilization and promote sustainable development. The country remains highly dependent on oil, which, during most of the past 55 years of its commercial exploitation, has contributed around 80 per cent of annual export earnings and 70 per cent of the revenue of the Government, with little variation over the years. However, this oil wealth has long been associated with internal conflicts, Dutch disease, environmental damage and economic mismanagement (Sala-i-Martin and Subramanian, 2003). By 2015, following a significant drop in oil prices, Nigeria was facing one of the worst economic crises in its history. Nigeria accounts for an estimated 46 per cent of the capital flight on the continent, based on average estimates for 2013–2015, and 80 per cent of the capital flight in Western Africa. In 2013, estimated capital flight peaked at $45.5 billion, or roughly $264 per capita. Capital flight in Nigeria increased to roughly 8.8 per cent of GDP in 2013 and, in 2015, despite some reduction, mainly due to declining oil prices, capital flight remained a significant problem (figure 27). In the same period, capital formation fell continuously, from 34 per cent of GDP to 15 per cent of GDP in 2015 and Government revenue declined from 27.6 per cent of GDP to 7.6 per cent of GDP. This trend presents a challenge in promoting structural transformation, economic diversification and social development and in reducing poverty and inequalities. Capital flight may be negatively associated with economic growth in the long term (Uguru, 2016; Ogbonnaya and Ogechuckwu, 2017). The literature on IFFs and economic development in Nigeria provides a diverse picture, yet there are more studies identifying a significantly negative impact (Olatunji and Oloye, 2015; Uguru, 2016; Ogbonnaya and Ogechuckwu, 2017; Nelson et al., 2018).
Figure 27
Nigeria: Capital flight, capital formation and Government revenue
(Percentage of gross domestic product)

Tackling IFFs in Nigeria has been a challenge. Significant efforts have been made to implement the necessary instruments to increase transparency in the oil and gas sector and to deal with IFFs.

Extractive industry transparency initiative
In 2003, Nigeria was the first country in Africa to join EITI and, in 2007, through an act of the National Assembly, established the Nigeria Extractive Industries Transparency Initiative as a transparency, accountability and anti-corruption initiative. The Initiative, an agency of the Government, is an autonomous self-accounting body with statutory reporting requirements to the President and the National Assembly. It is led by an executive secretary and overseen by a chair of the board. The Initiative is built on the principles and criteria of EITI and Nigeria was the first English-speaking country in Africa to be awarded satisfactory status by the board of EITI for implementing all requirements in the latter’s standards. The Initiative has been effective in strengthening public debate and promoting policy options with regard to signing bonuses, unpaid royalties and the theft of crude oil and refined products. It has identified $9.8 billion owed to the Government, of which $2.4 billion has

Source: UNCTAD calculations based on UNCTAD statistics, the ICTD and UNU-WIDER government revenue database and the Political Economy Research Institute database.
been recovered through the efforts of the Initiative (Tan and Faundez, 2017). The Initiative discloses data on the allocation of licences, the administration of oil and gas subnational transfers and crude oil sales within the Nigerian National Petroleum Corporation.

In February 2019, the report of the Board of EITI on the second validation of Nigeria cited information and data from reports of the Nigeria Extractive Industries Transparency Initiative and noted that around $3 billion in mostly illicit payments had been recovered.\(^{75}\) In 2020, the Nigeria Extractive Industries Transparency Initiative established a beneficial ownership register for extractive industries, which shows the beneficial owners of assets in the oil and gas sector; through the portal, the Government aims to track the origin of such funds that leave the country and to detect tax evasion, cases of money-laundering and drug financing.\(^{76}\) However, the registry may not have the desired comprehensive effect, as the legal instruments to make it enforceable may be lacking. A petroleum industry bill that seeks to unbundle the Nigerian National Petroleum Corporation and make the oil and gas sector more transparent may be passed by the National Assembly in 2020, attracting more investment into the sector.\(^{77}\)

**Tax reforms and financial transparency**

Nigeria has signed international treaties and agreements to tackle international tax avoidance and evasion. In 2017, Nigeria signed the Multilateral Convention to Implement Treaty-Related Measures to Prevent Base Erosion and Profit Shifting and the Common Reporting Standard Multilateral Competent Authority Agreement, which forms part of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters. Several national initiatives have been undertaken by the Government to tackle IFFs, as follows:

(a) Finance Act 2020, which came into force on 13 January and replaces Finance Act No. 30 of 1999 and is aimed at improving sustainable increases in public revenue and ensuring that tax law provisions are consistent with national tax policy objectives;

(b) Voluntary assets and income declaration scheme, introduced in 2017 to give defaulting taxpayers an opportunity to fulfil outstanding tax obligations from 2011–2016 without liability to penalty, interest or criminal prosecution. The limited success of this scheme can be related to the inadequate structure and processes for collaboration between regional tax authorities and the absence of a credible threat of post-amnesty proceedings;\(^{78}\)

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76 See https://allafrica.com/stories/201912090630.html.
77 See www.oilreviewafrica.com/events/event-news/nigeria-set-to-take-leap-forward-on-petroleum-industry-bill.
(c) Bank verification number scheme, introduced by the Central Bank in 2014 as a centralized biometric identification system for account holders that provides a unique identity for each account holder and protects the accounts of customers from unauthorized access; as at 2 February 2020, more than 40 million account holders had obtained bank verification numbers. The Government stated that it would freeze the accounts of those that did not obtain numbers. The scheme has achieved a high rate of compliance by account holders.

Another notable development in tackling IFFs through financial transparency is the improved inter-agency relationship between regulators, which has led to the recovery of funds for the Government. For example, the Economic and Financial Crimes Commission has established a dedicated tax investigation team to work with the Federal Inland Revenue Services and the Revenue Mobilization Allocation and Fiscal Commission in identifying and prosecuting tax evaders. The partnership involves information-sharing to arrest and prosecute tax defaulters in the country, in particular following the conclusion of the voluntary assets and income declaration scheme. Collaborative efforts by the agencies in the collection of outstanding value-added tax and withholding taxes led to the recovery of ₦28 billion ($77.56 million) in 2017.

Nigeria is among the most active countries in recovering stolen assets and engaging with multilateral stakeholders. Practical steps taken by the Government to address IFFs include the signing of bilateral agreements with Switzerland, the United Arab Emirates, the United Kingdom and the United States for the return of stolen assets, with the expectation that such bilateral agreements will act as a disincentive to the sending of illicit funds from Nigeria to these countries. The outcomes will depend in part on how the agreements are enforced and whether they dissuade corrupt practices. Most recently, the Government announced that it will reclaim $311 million in misappropriated funds, as part of an agreement with the United States and Jersey. The Financial Intelligence Unit is a central independent body within the Central Bank, responsible for requesting, receiving, analysing and disseminating financial intelligence reports, and its efforts have led to improvement in detecting cases of money-laundering, financing related to terrorism and other economic and financial crimes.

79 See https://nibss-plc.com.ng/bvn/.
81 See https://thenationonlineng.net/firs-teams-up-with-efcc-to-tackle-high-profile-tax-defaulters/.
According to reports by the Intergovernmental Action Group against Money-Laundering in West Africa on the implementation of the IMF Anti-Money-Laundering and Combating the Financing of Terrorism framework by member States, Nigeria has made notable progress, improved financial institutions and enhanced supervision, yet deficiencies remain in countering the financing of terrorism, investigating suspicious transaction reports, freezing funds or other property and convicting the financing of terrorism. Money-laundering is mostly conducted through investment in real estate and cross-border cash movements and through bank transactions. In 2014, the Financial Intelligence Unit received 1,442 suspicious transaction reports, but there were a low number of prosecutions (Intergovernmental Action Group against Money-Laundering in West Africa, 2014). Of the 477 cases detected through the suspicious transaction reports in 2018, 383 were related to money-laundering; none of the cases reported were processed (Intergovernmental Action Group against Money-Laundering in West Africa, 2018).

Federal Ministry of Finance whistle-blower programme

Nigeria introduced a whistle-blower policy in 2016 through an executive order of the Government, which seeks to incentivize the exposure of stolen funds in Nigeria and abroad and to reward whistle-blowers for tips that lead to the successful recovery of illicit funds (Gholami and Salihu, 2019). This anti-corruption programme encourages the voluntary disclosure to the Federal Ministry of Finance of information about fraud, bribery, financial misconduct and any other form of corruption or theft. Anyone responsible for providing the Government with information that directly leads to the return of stolen or concealed public funds or assets may be entitled to anywhere between 2.5 and 5.0 per cent of the amount recovered. The policy has led to some success. As at November 2019, the Government had saved ₦594 billion ($1.65 billion) through the policy since its introduction.

However, the policy has fallen short of its full potential given the absence of a statutory framework (Onuegbulam, 2017). Whistle-blowers are concerned about the risk of retaliation from employers if they provide information to the Government (Ifejika, 2018). The Government states that it deals with reports in a confidential manner and discourages retaliation against whistle-blowers, yet there is no legal protection for whistle-blowers (Omojola, 2019). In addition, there are no established penalties for those who retaliate against whistle-blowers and some have lost their jobs after reporting to the Government. Citizens are reluctant to become involved due to the lack of effective protection, as whistle-

87 See https://allafrica.com/stories/201911220105.html.
88 See https://www.pplaaf.org/country/nigeria.html.
blowers have faced a number of reprisals, ranging from suspension from work and the withholding of salaries and promotions to threats to their lives. To address such issues, in 2017, the African Centre for Media and Information Literacy launched Corruption Anonymous, a platform for protecting whistle-blowers and expanding the frontiers of whistleblowing as a mechanism for tackling corruption in Nigeria.

Despite recent efforts and improvements, in 2019, Nigeria ranked as the twelfth most vulnerable country on the Basel anti-money-laundering index with regard to money-laundering and terrorist financing risks, out of 125 countries, down from a rank of sixteenth in 2018. Nigeria has made some improvements, and progress is observed in voice and accountability, as efforts to increase transparency and freedom of speech seem to have been fruitful and, after 2014, some progress was observed in the control of corruption, yet Nigeria ranks among the lowest in political stability. Security is crucial to socioeconomic development and insurgency and terrorist activities remain serious threats (Yagboyaju and Akinola, 2019).

6.7 Concluding remarks

Countries in Africa raise less tax revenue as a share of GDP than countries in other regions. In light of high levels of capital flight and tax avoidance and a relatively high level of dependence on corporate income tax, countries in Africa face significant limitations in increasing tax bases. The significant financing gap related to achieving the Sustainable Development Goals cannot be closed solely through Government revenue. Within the context of AfCFTA and regional economic communities, enhanced regional cooperation among countries in Africa could potentially have an important role in raising greater tax revenue from extractive industries in the following ways:

(a) Intra-African coordination and cooperation by tax administrations and cross-border prosecution of crimes;

(b) Elaboration of regional positions and proposals as a contribution to global tax cooperation efforts in existing institutional contexts;

(c) Joint programmes and mutual support towards capacity-building in tax administration and enforcement.

The comparison in this chapter between estimated financing needs and levels of capital flight suggests that countries in Africa could contribute to closing the financing gap by
tackling IFFs. An integrated financing approach targeting several sectors, considering multiplier effects across various Goals and related targets, is crucial to increasing the effectiveness of current spending on health and education. Country-specific evaluations are necessary in order to identify national Goals-related needs, financial requirements and leakages, to improve spending efficiency. In order to tackle IFFs, transparency in extractive industries, multilateral cooperation in stolen asset recovery, financial investigations and dealing with corruption have shown some measure of successful results.