# ATI partner countries' perspectives on tackling tax related illicit financial flows (TIFFs)

*ATI General Assembly - Consultative Group 3 Meeting*

**Lusaka - Zambia**

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**21 June 2023**

# Agenda

- Background
  - Objective
  - Scope of the study
  - Methodology
  - Summary of literature review
- Indicators to assess ATI partner countries
  - Main indicators
  - Specific areas of assessment
- ATI partner countries' experiences
  - Transparency and EOI
  - Transfer (mis)pricing
  - Trade mis-invoicing
  - Interagency cooperation
- Conclusions and recommendation
  - Conclusions
  - Holistic approach
  - Capacity building
  - International cooperation

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# Background: Objective and scope of the study

- **Objective**
  - Sharing best practices, lessons, successes and challenges in combating TIFFs among ATI partner countries

- **Scope of the study – TIFFs**
  - No international consensus on the definition, component and scope of IFFs/TIFFs

Financial resources crossing borders that are illegally earned, transferred or used abroad

Financial resources crossing borders that are illegally or illegitimately earned, transferred, used or concealed abroad

- IFFs: illegal *vs* illegitimate
- TIFFs: tax evasion *vs* tax avoidance

+ cross-border flows

Illegal or illegitimate due to the origin or destination of the fund or the method of transfer

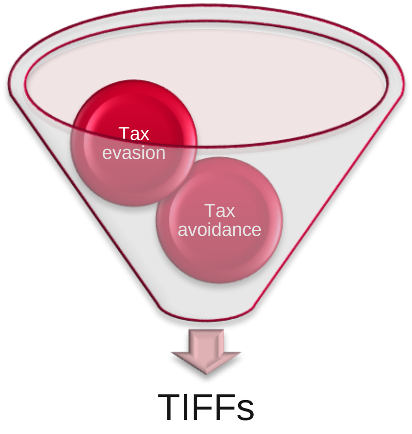
# Background: Objective and scope of the study … continued

## Scope of the study – TIFFs

- Adopted definition for IFFs and TIFFs

**IFFs**: Financial resources – whether obtained illegally or illegitimately – crossing borders or transferred, used or concealed abroad with the intention of hiding them from the tax authorities of the involved jurisdictions.

**TIFFs**: Any abusive tax practice that undermines the object and purpose of a tax system and (i) deprives countries of resources that could be used for financing public goods; (ii) fosters inequalities; and (iii) undermines trust in the government. These practices include tax evasion and tax avoidance, such as  transfer mispricing and trade mis-invoicing.



# Background: Methodology

## Methodology

| Desk research | Questionnaire | Interview |
|---|---|---|
| • Set a foundation for common understanding on IFFs and TIFFs for the purpose of this study<br>• Assessed global, regional and national perspectives, challenges and initiatives<br>• Analysed relevant policy recommendations and non-ATI countries' practices | • Sent out to all ATI partner countries (25 by then)<br>• 13 countries responded | • Pakistan, Rwanda and Tanzania<br>• Indonesia and Kenya submitted written answers |

# Background: Summary of literature review

- **Revenue implications**
  - There are no methodologies to accurately quantify the impact of IFFs/TIFFs
  - However, there is a range of estimations of revenue forgone made by different studies

| Study | Time | Estimated outflow through IFFs | Category of countries | Remark |
|---|---|---|---|---|
| **GFI (2015)** | annually | USD 500 billion | Developing countries | |
| **GFI (2013)** | Annually<br>2002 - 2011 | USD 946.7 billion in 2011 (10% per year)<br>USD 5.9 trillion | 55 Developing countries | Asia (39.6%), EU (21.5%), West Hemisphere (19.6%), MENA (11.2%) and Africa (7.7%) |
| **AU/UNECA HLPR (2015)** | Annually<br>Over 50 years | USD 50 - 60 billion<br>> USD 1 trillion | Africa | Equivalent to all ODA received |
| **AUC (2019)** | Annually | USD 50 - 80 billion | Africa | |
| | | **Loss in tax revenue through TIFFs** | | |
| **IMF (2015/16)** | Annually | USD 600 billion | Globally | USD 400 billion OECD<br>USD 200 billion others |
| **UNCTAD (2015)** | Annually | USD 100 billion | Developing countries | |
| **Christian Aid (2015)** | Annually<br>2000 - 2015 | USD 160 billion<br>USD 2.5 trillion | Developing countries | |
| **TJN (2017)** | Annually | USD 130 billion | Globally | By US MNEs tax avoidance alone |
| **>>** | Annually | > 20% tax revenues | 20 developing countries | ATI partner countries: Pakistan (39.68%), Sierra Leone (26.57%), Tanzania (21.16%) and Uganda (22.17%) |
| | | **Trade misinvoicing** | | |
| **GFI (2021)** | 2009 - 2018 | USD 1.6 trillion value gap in 2018 alone | 134 developing countries | |
| **GFI (2013)** | 2002 - 2011 | Average IFFs USD 542 billion per year and 80% through trade misinvoicing | 55 Developing countries | |
| **AU/UNECA (2015)** | 2001 - 2010 | USD 407 billion | African countries | |
| **GFI (2011)** | 2001 - 2010 | USD 242 billion | Developing countries | |

# Background: Summary of literature review

## Challenges

| Global | Continental/Regional | National |
|---|---|---|
| ▪ Limited or overlapping and uncoordinated mandates at international level<br>▪ Complex procedures underpinning international cooperation | ▪ Lack of coordinated legal and institutional framework<br>▪ Complex procedures underpinning continental or regional cooperation | ▪ Inadequate regulatory frameworks<br>▪ Lack of human and technological capacities<br>▪ Duplication of functions and lack of coordination among different agencies |

## Initiatives

**Global**

- UN GA Resolution/2021 and UN SG report/2022
- Global Forum Transparency and EOI; Model TIEA; MAATM MC; BEPS Project
- OECD/UN TP and DT MC; UNCTAD and UNODC framework and guidance to measure IFFs; GFTrade assessment tool

**Continental /Regional**

- AU subcommittee on Tax and IFFs; African Initiative 2015; Yaoundé Declaration
- Asian Initiative (Bali Declaration) 2021/22; Latin America Initiative (Punta del Este Declaration) 2018

## Policy recommendations

- OECD's fighting tax crime – Ten global principles
- GFI and others – Accelerated IFF agenda in Africa
- FATF recommendations
- AU/UNECA HLPR on IFFs from Africa
- ATAF – Six pilar approach to combat IFFs

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# Indicators to assess ATI partner countries' perspectives against TIFFs

**Main indicators of the assessment**

1. **Policy and legal framework**
2. **Institutional framework**
3. **Interagency cooperation**
4. **Capacity building**
5. **International cooperation**

**Specific areas of assessment**

1. Policies and strategies against TIFFs
2. Tax abuse (i.e. tax evasion & tax avoidance)
3. Transfer (mis)pricing
4. Trade misinvoicing
5. Transparency and exchange of information
6. Capacity building
7. Interagency cooperation
8. Stakeholders' engagement

Practices | Successes | Challenges | Next steps

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# ATI partner countries' experience: Transparency and EOI – Practices

## Indonesia

➢ **Domestic law**
- BO information of entities and arrangements through AML
- EOI provisions in KUP law and regulations (2017) – also deal with EOI with other countries
- Broader access to domestic information automatically/ by request

➢ **International instruments**
- 69 out of 71 DTAs contain EOI provisions
- Signatory to MAATM MC, TIEAs, MCAA and BCAA on AEOI CbCR and financial account information (CRS)
- Joined the Global Forum and Asia Initiative
- Bilateral MoUs on withholding taxes
- Uses commercial data

➢ **EOI unit and enforcement**
- DGT-DIT-EOI unit 30 staff
- Required IT infrastructure for EOI is in place
- Commenced exchange under the AEOI standard in 2018

## Kenya

➢ **Domestic law**
- BO requirement through the Companies Act 2017/ Companies (BO information) Regs. 2020
- EOI provisions in ITA and TPA – also deal with EOI with other countries
- Finance Act (2021) and Tax Procedures Regs (2023) on AEOI(CRS)
- Broader access to domestic information

➢ **International instruments**
- 15 DTAs contain EOI provisions and only eight up to international standards
- Signatory to MAATM MC and MCAA on AEOI, CbCR and CRS
- Joined the Global Forum and Africa Initiative

➢ **EOI unit and enforcement**
- KRA-ISOD-EOI unit 10 staff and adequately resourced
- KRA obtain information from government agencies such as BRS and FRC, and from financial institutions
- KRA has been implementing EOIR since 2018 and committed to implement the AEOI standard in Sept. 2023

# ATI partner countries' experience: Transparency and EOI – Practices

## Pakistan

**Domestic law**
- BO - Finance Act 2022 introduced definition of BO into Income Tax Ordinance (ITO) and Company Act 2017 also deals with BO
- EOI provisions in ITO, Sales Tax Act and other tax acts. ITO also deals with EOI with other countries
- Broader access to domestic information

**International instruments**
- 66 DTAs contain EOI provisions
- Signatory to MAATM MC and MCAA-AEOI (or AEOI-CRS)
- Joined the Global Forum and Asia Initiative

**EOI unit and enforcement**
- FBR-DGIT – six offshore commissionerates/tax offices
- Automated information exchange platform between Inland Revenue Services and Customs Services
- FBR database integration with the national database and registration authority (NADRA)
- Data sharing agreement between FBR and provincial authorities underway to build robust database
- Commenced exchange under the AEOI standard in 2018

## Uganda

**Domestic law**
- BO – ITA
- EOI provisions in TPA, ITA, VAT regs and Stamps Act – also deal with EOI with other countries
- March 2023 – issued bill to implement MAATM MC
- Broader access to domestic information

**International instruments**
- Nine DTAs contain EOI provisions
- Signatory to MAATM MC and MCAA on AEOI financial account information,
- Joined the Global Forum and African Initiative
- Signatory to ATAF-AMATM and member of EAC-CMA

**EOI unit and enforcement**
- URA – has a dedicated EOI Unit operational since 2016
- Committed to implement the AEOI standard by 1 Sept. 2023
- Agencies have signed MoUs to facilitate sharing of information between different law enforcement authorities

# ATI partner countries’ experience: Transparency and EOI – Successes

**Kenya**

- Since 2017 sent out 382 EOIR and received 160 responses and in 2018 received 122 EOIR
- Actively engage on international forums on EOI
- KRA able to identify additional revenue approx. **KES 1.5 billion**
- KRA staff’s awareness increased on EOI options
- **Next** – automatization of EOI procedures (now manual)

**Uganda**

- Uganda made 69 EOIRs between 2014 and 2019, up from only two in 2012, and identified nearly **USD 26 million** in additional revenues.
- Until the end of 2022, Uganda had realized significant revenues from EOI i.e**. USD 96.5 million**.

**Pakistan**

- From 2018-2020 FBR generated more than 1000 EOIRs
- FBR received AEOI-CCRS in 2018 from 27 jurisdictions, in 2019 from 55 jurisdictions and in 2020 from 49 jurisdictions
- In a nutshell FBR received financial information from 86 countries and sent to 66 countries
- EOI is playing a very significant role in revenue mobilization and enhanced tax investigation potential
- FBR **identified USD 27 million** potential unpaid tax revenue and managed to collect around **USD 6 million** due to EOI via MAATM MC.

**Indonesia**

- From 2017-2021 received 376 letters containing information through EOIR from others states and sent 118 EOIR letters
- Improves tax compliance
- Assists DGT on tax examinations and compliance assessments
- Helps Indonesia **boost its tax revenue** and tax avoidance schemes by **detecting noncompliant taxpayers** and **discovering hidden offshore assets and unreported income**

# ATI partner countries' experience: Transfer (mis)pricing − Practices

## Indonesia

➢ **Legal framework**

- Transfer pricing (TP) related provisions in different tax legislation including in the ITA, VAT Act and MoF regulations of 2016 and 2022
- TP regulations vary depending on the administrative nature of the issues
- TP policy and documentation i.e. Local File, Master File and CbC report as part of CIT return
- No specific TP penalties due to the nature of the TP regime but general tax principles in satisfying CIT and VAT obligations would apply
- Therefore, any violation of these rules will be subject to KUP law including TP adjustment and criminal liability
- DGT – Indonesia's TP regulations are designed to conform with BEPS Actions 8-10 and 13 as well as the OECD TP Guidelines.

➢**TP unit and enforcement**

- DGT has several tax units that are engaged in TP issues
- These tax units deal with TP issues by formulating policies and strategies on TP and implementing APA and MAP, processing TP and CbCR data, supervision and assessment of TP cases
- DGT has TP Knowledge Centre since 2020 and its functions include coordinating, assisting and building the capacity of the tax officials in handling the TP cases
- Uses internal and external databases for comparables

## Rwanda

➢ **Legal framework**

- TP rules have been included in the legal framework since 2005 but actual implementation started in 2019 and became effective in 2020
- TP policy and documentation i.e. Local File, Master File and CbC report along with CIT return
- 2% WHT on certain payments to related but non-resident persons
- Any violation of TP rules is punishable by administrative fines and/or criminal penalties on tax evasion

➢**TP unit and enforcement**

- RRA – ITU established in 2018 deals with TP and other international tax issues
- RRA has its own system to obtain basic information which helps in the risk profiling of TP cases. But has not built its own database yet
- Uses internal and external database for comparables

# ATI partner countries' experience: Transfer (mis)pricing – Successes

**Rwanda**

- RRA has managed to conclude eight TP cases and correct tax by using external database
- It is collecting more taxes now through TP adjustment
- **Nex**t – expanding the TP team in the ITU unit within RRA, building internal database and continuing using more external databases for comparability analysis

**Indonesia**

- Increasing tax revenues through TP adjustment and litigations and more compliance
- DGT optimizes the use of the EOI instrument to obtain valid data and information related to the pricing of cross-border controlled transactions.
- The TP system is designed to tackle profit shifting and base erosion caused by non-arm's length price setting of controlled transactions
- It helps in addressing TIFFs although difficult to assess
- DGT has been continuously improving the capacity of its internal system in generating reliable data and information entailed for TP analysis
- **Next** – increasing the validity of TP adjustments, refining current TP regulations, notably on the aspects of TP audit and enforcement targeting vulnerable sectors (e.g. extractive sectors), to improve the effectiveness of the TP system

# ATI partner countries' experience: Trade misinvoicing – Practices

Dissolving pulp sent from Indonesia to China, 2007-2018


*Sources: Indonesia data for HS Code 470200 from Badan Pusat Statistik; China data for HS Code 470200 from UN Comtrade.*

China imported over 2 billion tons while Indonesia exported to China approximately 400,000 tons of same product during the same time

*Source* GFI (2021), *The Macao Money Machine: Profit Shifting and Tax Leakage in Indonesia's Pulp Exports*

- Intentional misstatement of the value, quantity or composition of goods on customs declaration forms and invoices presented by importers or exporters to customs agencies
- It occurs through:
  - import under-invoicing;
  - import over-invoicing;
  - export under-invoicing; and
  - export over-invoicing.
- Though it occurs through commercial invoices and customs declarations, the transfers and motivations involved are linked to cross-border tax evasion and tax avoidance i.e. TIFFs and money laundering.
- For example, import under invoicing ➡ affects the amount of VAT, customs duties, excise tax, surtax or any other tax on import ➡ disrupt continuous transactions with no/false invoice including VAT or sales tax ➡ evade CIT ➡ vicious circle
- TIFFs through trade misinvoicing pose the greatest threat to domestic revenue collection and foreign exchange earnings in many countries.

# ATI partner countries' experience: Trade misinvoicing – Practices

**Pakistan**

- **Legal framework**
  - Provisions to prevent trade mis-declaration or mis-invoicing under Customs Act, Sales Tax Act, ITO and AMLA
  - Tracking and trading mechanisms in the Sales Tax Act
- **Institutional set-up and enforcement**
- FBR is responsible for preventing, detecting, investigating and prosecuting trade misinvoicing
- Customs Service plays the main role in implementing the measures to curb trade misinvoicing
- FBR introduced a tracking and tracing mechanism to obtain real-time invoices as well as the number of invoices issued by the retailers by the name of the point of sale (POS)
- Tracking and tracing catalysts are being applied, starting from manufacturing processes
- Products are stamped electronically through unique product identifiers to counter illegally smuggled or not properly verified products and unstamped products will be confiscated by the FBR
- Input tax claims for domestic sales tax is conditioned on the traceability of the transaction chain
- Customs Service is partnering with other countries to implement an electronic data interface (EDI) to seek real-time value of the goods declaration (GD) from the trading partner country
- Have established mechanisms with a few countries (including China) to have an electronic exchange of data regarding imports and exports so that the true value is reported in the country where the goods are landing

**Rwanda**

- **Legal framework**
  - Provisions to prevent trade mis-declaration or mis-invoicing under Customs Act, VAT Act, EAC CMA and CMRs
  - VAT Act requires use of electronic billing machines (EBM) to issue invoices
- **Institutional set-up and enforcement**
- RRA – RIED is responsible for detecting, investigating and prosecuting any tax crimes including trade misinvoicing
- No VAT input refund claims unless invoices are issued by the using EBM i.e. traceability of transaction chain
- Customs Service investigate imports and exports by using ASCUDA ++ and adjust declaration to correct value to levy taxes and duties

# ATI partner countries' experience: Trade misinvoicing – Successes

## Rwanda

- ASYCUDA ++ helps mitigate revenue losses through trade misinvoicing and actual declarations have increased
- Next – to expand list of products under specification codes

## Pakistan

- The tracking and tracing mechanism has an immense impact on **countering trade misinvoicing** and contributes to **avoiding revenue leakages** and **countering new loopholes**.
  - For example, after the POS integration through the tracking and tracing mechanism, real-time reports of sales jumped on average to around PKR 70 million
- Exchange of customs data with other countries helps **combat TIFFs through trade misinvoicing** and **enhance revenue collection**
  - For example, before the implementation of electronic data interface (EDI) and the arrangement on electronic exchange of data (with China) there were substantial differences on customs data between Pakistan's and Chinese customs authorities regarding the same import/export. China reported that it had exported USD 3 billion of goods to Pakistan but Pakistan importers showed only USD 50 million to USD 1 billion

# ATI partner countries' experience: Interagency cooperation

## In general

- Most responding ATI partner countries mentioned that there are different government agencies that are working closely with tax authorities in combatting TIFFs
- They have interagency cooperation on an ad hoc basis on some tax-related issues but lack a consolidated approach
- However, none of them indicated the existence of a legal or formal framework for interagency cooperation against TIFFs

## Interagency cooperation under AML

- Most of the responding ATI partner countries have indicated that they have a task force under AML framework
- Purpose – countering money laundering and financing terrorism
- Scope – it is confined to proceeds from criminal activities
- However, it can pave the way or serve as a starting point to have a similar framework against TIFFs

## Rwanda

- A committee, involving the RRA, was established to address gaps identified by the Global Forum (2020) on Rwanda laws
- Initiative/MoU on collaboration in matters related to cross-border cash and other instruments among several agencies
- MoU signed between particular institutions to combat money laundering
- Next – Rwanda will work on this to consolidate the cooperation among the relevant government agencies following the recommendations of this study.

# ATI partner countries’ experience: Challenges

Limited level of awareness about IFFs/ TIFFs and lack of political commitment

DRM strategies, AML policies and NRA strategies but no TIFFs as a threat

Absence of appropriate laws and dedicated units on TP, EOI and Trade MI

Capacity limitation to assess the prevalence of IFFs/TIFFs and revenue loss

Absence of systematic interagency cooperation on TIFFs and international cooperation

Lack of comparable data or information for TP, Trade MI and other tax abuses

Capacity limitation in implementing/ understanding TP rules and available

Need for more specialized training on TP, EOI, and other international tax issues

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# Conclusions

Level of awareness on TIFFs is inadequate

DRM strategies and national development policies/plans of ATI partner countries have not identified TIFFs as a threat to DRM efforts

Existing legal frameworks deal with almost all the components of TIFFs in the form of tax evasion, tax avoidance, transfer mispricing and rarely trade mis-invoicing

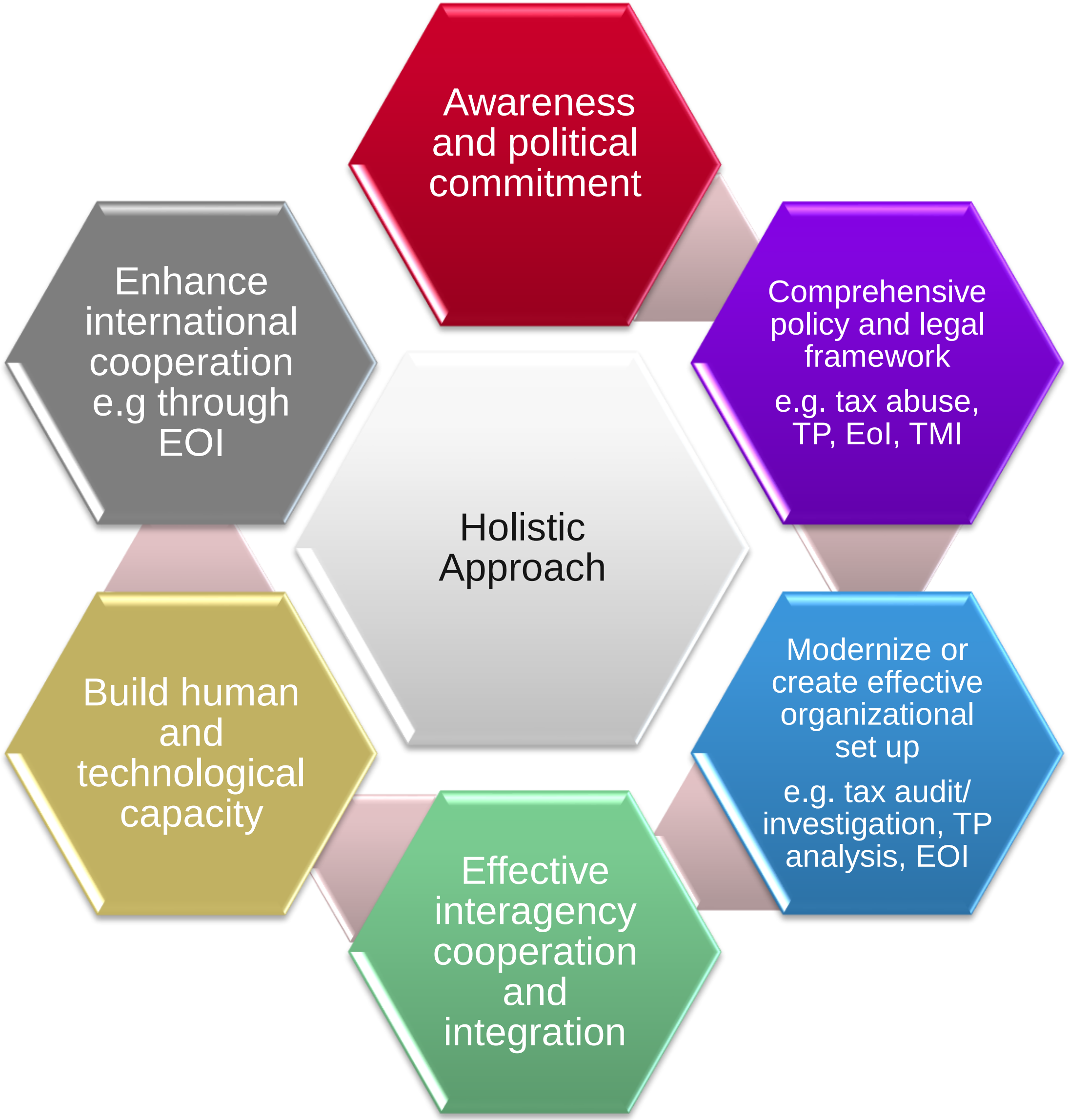
ATI partner countries’ initiatives on TP and EOI including commitments to international cooperation are encouraging despite a range of differences in domestic provisions and level of enforcement

The impact of trade misinvoicing is not well addressed

The level of interagency cooperation in combatting TIFFs is insufficient

There are human and technological capacity limitations

# Recommendation: Holistic approach to effectively tackle TIFFs



# Recommendation: Capacity building and international cooperation

## Capacity building

### Human capacity

- Interpretation and application of tax treaties
- TP rules and their applications in cross-border transactions
- BO and EOI options, standards, principles and their application
- Tax audits and investigation techniques including best practices in managing tax cases
- Methodologies to measure prevalence of, and revenue loss through, IFFs/TIFFs
- Implementation of best practices and recommendations to combat TIFFs

### IT infrastructure

- Data/information gathering
- Implementation of EOI options
- TP analysis
- Trade misinvoicing analysis i.e. tracking and tracing

## EOI and international Cooperation

### Bilateral

- TIEAS
- DTAs

### Multilateral

- MAATM MC
- Global Forum and regional initiatives
- ATAF-AMATM

# Thank you for your attention!

# Questions?

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