UNITED NATIONS
HUMAN RIGHTS
OFFICE OF THE HIGH COMMISSIONER

Financing Development For All By Curbing Illicit Financial Flows

QUICK FACTS

- Developing countries lost approximately $7.8 trillion in illicit financial flows from 2004 to 2013. 87.4% of all illicit financial flows are caused by transfer mispricing, or the fraudulent misinvoicing of trade in cross-border tax-related transactions.

- $161.6 billion was received by African countries in 2015, primarily through loans, personal remittances and aid. Yet, $203 billion was extracted, mainly through transnational corporations repatriating profits and illegally moving money out of the continent.

- Every $100 million in stolen assets recovered could fund first-line treatment for over 600,000 persons with HIV/AIDS for a year or some 250,000 water connections for poor households.

- Developing countries collect between 10 to 20% of their GDP through tax revenue, whereas developed countries collect between 30 to 40%.

Illicit financial flows distort economic and political competition, subvert government institutions, generate conflicts and undermine the integrity of legal and financial systems.

Aggressively tackling illicit financial flows is key to mobilizing the funds needed to make progress on the Sustainable Development Goals

THE PROBLEM

Illicit financial flows are movements of money or capital from one country to another, or funds that are illegally earned, transferred, and/or utilized across an international border. The term includes tax evasion and tax avoidance schemes by transnational corporations, money laundering and transfer of funds from bribery, corruption and criminal activities.

Illicit financial flows prevent low-income countries from mobilizing and spending significant public financial resources required for inclusive and equitable social and economic development. They also often constitute a way to illegally transfer much-needed financial resources from developing to developed countries and consequently exacerbate existing inequalities.

The loss of potential public funds through illicit financial flows within and across countries and the consequent reductions in public sector investments, as well as the amplification of foreign debt burdens, reduce and impair the capacity of States to invest in social sectors vital to sustainable development, particularly health and education, or in human rights terms, the rights to health and to education. In order to compensate for revenue shortfalls, regressive tax measures such as consumption taxes and other forms of indirect taxes are implemented. Indirect and consumption taxes disproportionately affect the income of low-income households and their ability to purchase basic goods and access public services.

When public services are absent, the additional costs and labour of unpaid care work, as well as informal sector work, are often placed on women and girls. Public services, such as water, may be privatized, posing problems of affordability and accessibility. The World Health Organization specifies 50 litres of water per person per day as the recommended quantity needed to maintain health, hygiene and for all domestic uses. For poor people in the developing world with no access to safe public water, buying the recommended 50 litres a day from expensive private vendors can be a huge drain on their earnings. Many people have no choice but to compromise their health and dignity by using much less or collecting water from unsafe sources. When they get sick from waterborne deseases, they cannot afford the cost of private hospitals and rely on inadequate public healthcare systems, further jeopardizing their health and wellbeing. Thus, illicit financial flows create significant barriers to basic human rights including the rights to water and health and to the attainment of the Sustainable Development Goals.

Low- and middle-income countries tend to be more reliant on corporate income tax as a share of all tax revenue than are higher income countries, have fewer realistic alternative source of revenues, and financial losses they face through corporate tax avoidance are often in the higher proportions of their gross domestic product.

An important driver of low corporate taxation is the phenomenon of global tax competition, whereby primarily developing countries offer tax incentives, concessions and exemptions to transnational corporations as a bid to attract foreign direct investment, particularly in the manufacturing and services sector, including financial services. Tax evasion and/or repatriation of profits by transnational companies operating in developing countries, in contrast to national taxation of domestic companies, creates an inequality where foreign firms often gain greater competitiveness, profits and financial power than domestic firms. The majority of domestic firms cannot take advantage of cross-border tax haven transactions in order to lower their taxes, deepening inequalities between high, low- and middle-income countries. Thus, combating illicit financial flows is both an imperative and a fundamental means for achieving the Sustainable Development Goals and to fully realising all human rights.

POTENTIAL SOLUTIONS

The right to development

The right to development aims to create an enabling environment for development, peace and human rights, and the mobilization of resources for sustainable development. Under the Declaration on the Right to Development, all human beings have a shared responsibility for development, taking into account the need for full respect for their human rights and fundamental freedoms as well as their duties to the community. States whose business enterprises are responsible for illicit financial flows are obligated under the Declaration to cooperate internationally to address the impacts of the actions of the business entreprises on developing countries in which they operate. The inherently international dimensions of this right are based on the notions of a common humanity, invoke shared global responsibilities of States and mutual accountability of the international community across national boundaries. Pursuant to the right to development, States have obligations at three levels: (a) internally, through the formulation of national development policies and programmes affecting persons within their jurisdictions; (b) internationally, through the adoption of policies extending beyond their jurisdictions; and (c) collectively, through global and regional partnerships.

Policy recommendations

- Enforce the automatic exchange of tax information, beneficial ownership, country-by-country reporting, conducive and gender-sensitive tax policies at the State level. Promote transparent access to data on illicit financial flows, human rights impact assessments, international and regional cooperation, capacity building for national tax administrations and reassessing the Doing Business Indicators for international organisations.

- Implement the Addis Ababa Action Agenda to substantially reduce illicit financial flows and systematic tax evasion by international corporate actors by 2030, with a view to eliminating them over time in all countries.

- Establish a democratic, inclusive, and transparent Global Tax Body under the auspices of the UN. Strengthen advocacy on enhancing global financial transparency and international cooperation for tax governance.

In most developing countries, the ability to raise revenue domestically is not only a function of domestic policies and institutions but is also significantly shaped by international tax norms, the global policy environment, and the prevalence of illicit financial flows through international tax avoidance and evasion practices. The current global tax regime lacks effective penalties and clear international regulations, thereby promoting tax competion between countries while facilitating illicit financial flows.

CONTACT

R2D@ohchr.org

www.ohchr.org

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