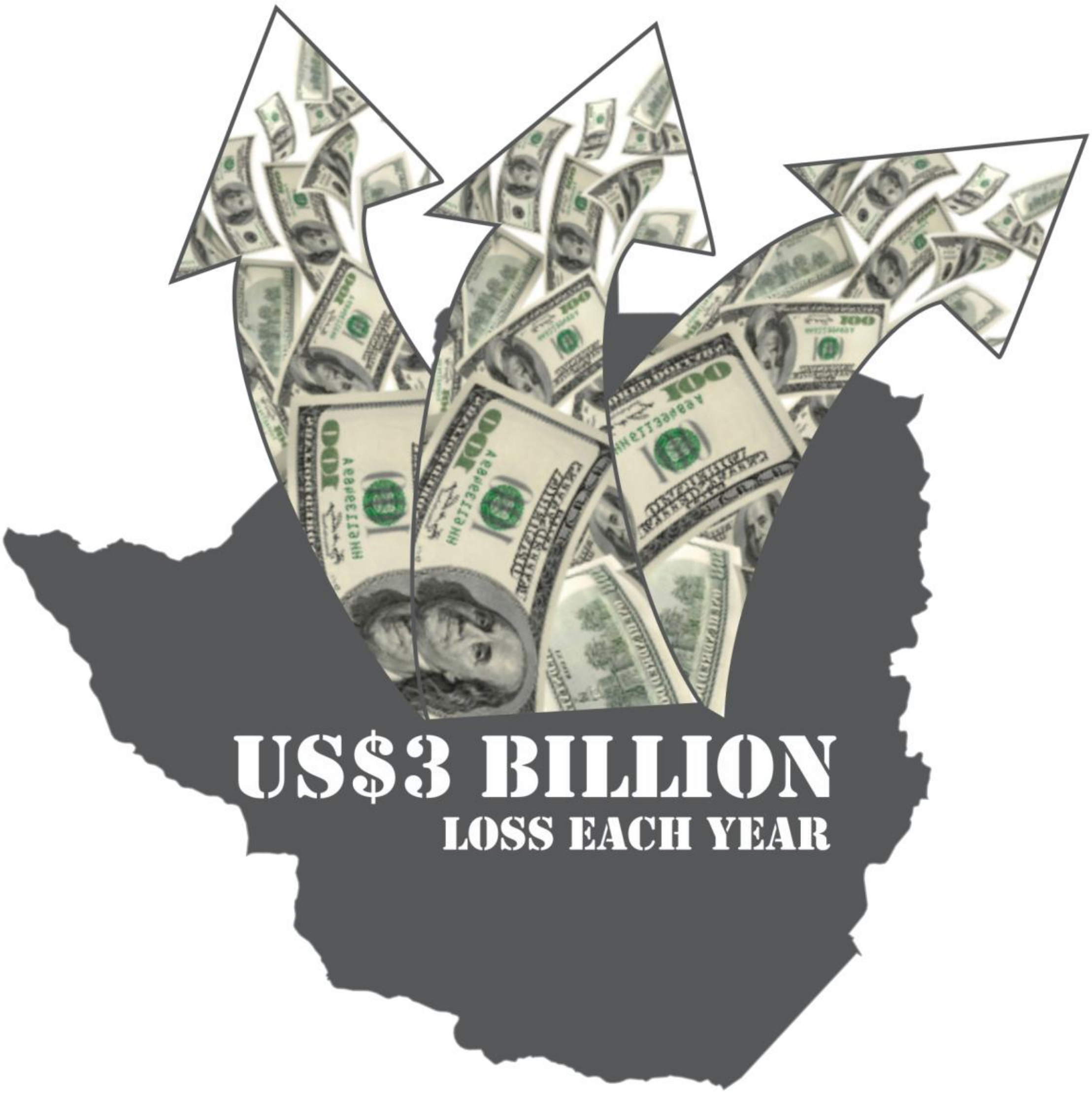
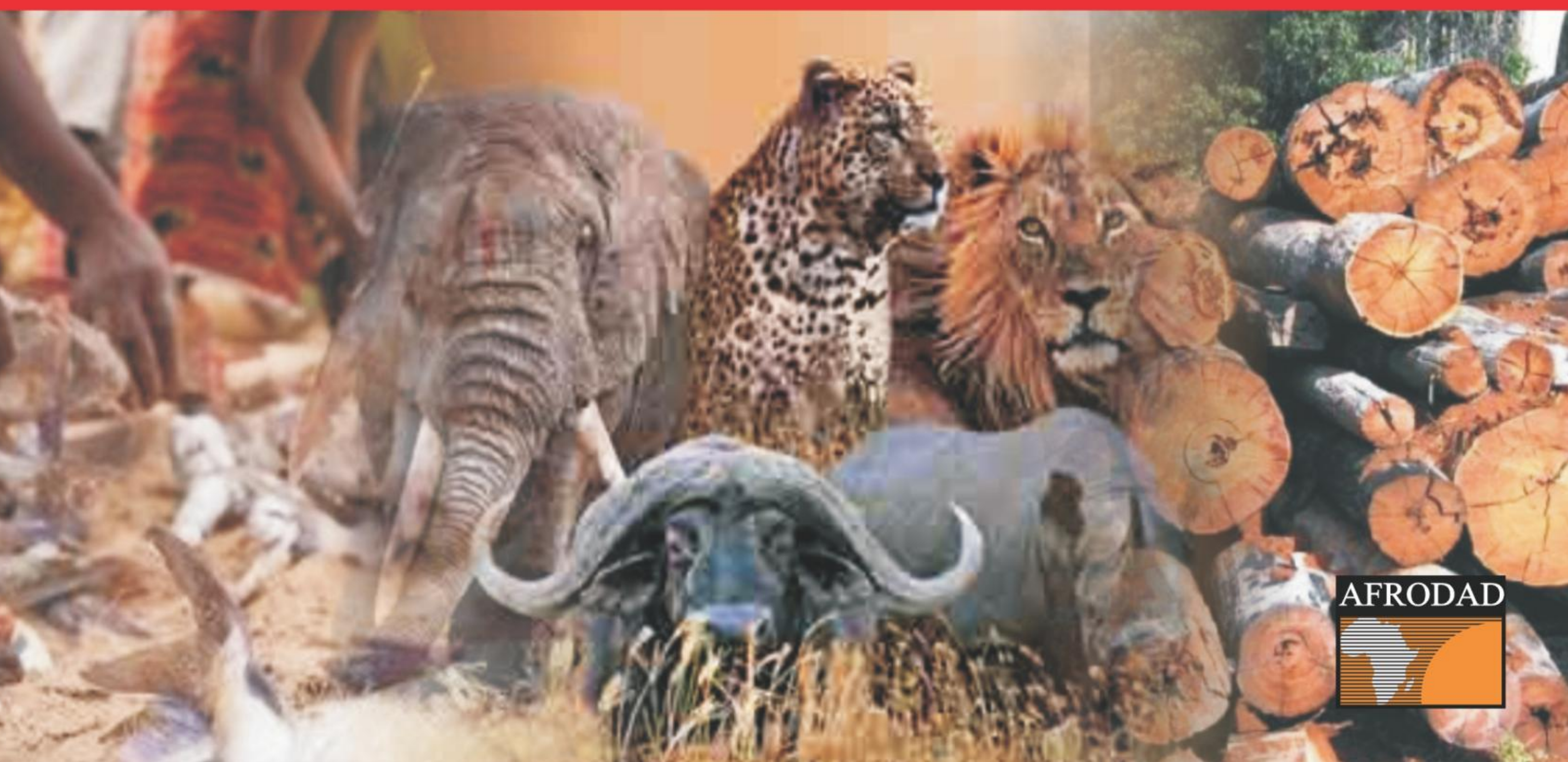


ILLICIT FINANCIAL FLOWS:

TOWARDS A MORE INTEGRATED APPROACH FOR CURBING ILLICIT FLOWS FROM ZIMBABWE



ILLICIT FINANCIAL FLOWS: TOWARDS A MORE INTEGRATED APPROACH FOR CURBING ILLICIT FLOWS FROM ZIMBABWE *(Abridged version)*

EXECUTIVE SUMMARY

This study is an attempt to estimate the levels of Illicit Financial Flows (IFFs) from Zimbabwe's Mining, Fisheries, Timber and Wildlife sectors, over the period 2009 to 2013. It seeks to assess the possible drivers of IFFs and the existing legal and institutional frameworks designed to curb IFFs. The study also provides rich background material on the legal and institutional frameworks governing the development and exploitation of natural resources in Zimbabwe. A comparison of national strategies within the Southern Africa region to combat illegal exploitation and trade of the resources from the aforementioned sectors is discussed, with a view to draw important lessons for Zimbabwe.

ABOUT THE STUDY

The study makes use of both qualitative and quantitative techniques to answer the research questions set out in the original Terms of Reference. It notes that IFFs are very complex and difficult to accurately measure, due to the fact that many illicit transactions tend to be settled in cash, as parties involved in such transactions eliminate any incriminating audit trails. Furthermore, transactions of this nature are never declared and it becomes extremely difficult to track and measure how much government revenue is lost through these malpractices. A number of methodologies that have been applied on the global scale to estimate IFFs are discussed: the IMF Reference Guide, the Residual Method by the World Bank and the Trade Mis-pricing Model. The study used the trade Mis-pricing Model, given that trade mis-invoicing is one of the key conduits, accounting for over 70% of IFFs, through which economic agents illegally move money out of (and into) developing countries. Furthermore, the Trade Mis-pricing model is ideal for sectoral analysis of the IFFs, which is what this study set out to achieve.

ESTIMATES

The estimates are based on the analysis of data sets for partner-country trade, covering the aforementioned sectors, from United Nations Commodity Trade Statistics Database (UNCOMTRADE) and Convention on International Trade in Endangered Species (CITES). The study estimated that between the period 2009 - 2013, Zimbabwe lost US$2.83 billion, through illicit flows, translating to an annual average of US$570.75 million. Of the cumulative outflows, 97.88% (US$2.793

billion) were in the mining sector. IFFs in wildlife accounted for 0,53%of the total, at US$15.07 million, whilst Fisheries and Timber accounted for 0.98% and 0.61% at US$28.04 million and US$17.30 million, respectively.

The most immediate impact of IFFs is a loss of revenue, hence, a loss of opportunities for domestic consumption and investment, both public and private. These revenue outflows could have been used for productive economic and social investments, in support of the economic growth objectives of the government. Redressing the net outflows from Zimbabwe, that we estimate at an annual average of US$570.75 million, (from 2009 to2013), could help create additional fiscal space for critical growth enhancing investments.

IFFs are mainly underpinned by a number of factors, chief among them being legal and institutional lapses in the domestic fiscal and financial systems, leading to corruption and other forms of trade mal-practices. Other key drivers of IFFs in the Wildlife and Fisheries sectors include, demand and supply mismatches, price mismatches resulting from price controls, tax and exchange control loopholes. Regarding the Mining sector, IFFs are mainly a result of corruption, dysfunctional regulation, weak enforcement of rules, tax evasion, tax avoidance, smuggling, lack of transparency and accountability in the collection and management of natural resource revenues. Furthermore, Government's limited information on the quantity and quality of geological deposits, and shortcomings of the Mines and Minerals Act [Chapter 21: 05], create room for rent seeking behaviour and under-declarations of quantity and quality of minerals, thus aiding the illicit outflows of money from the country.

With regards, to timber, the level of IFFs is low and is not a major cause for concern from a Fiscal revenue perspective. However, the major challenge with the timber sector is the rampant illegal logging of trees for domestic consumption. The underlying drivers are the weak enforcement of environmental policy and legal frameworks in addition to their inconsistencies, poverty, and very high unemployment in Zimbabwe that leaves people with limited alternative sources of livelihood. The other challenge is that of insecurity of land tenure, coupled with the ownership wrangle that accompanied the resettlement programme, exposed indigenous forests to illegal exploitation.

A review of national strategies to combat IFFs in the Southern Africa region shows that a number of countries have instituted varied legal and institutional arrangements. For example, countries have enacted Anti-corruption Acts, Anti-Money Laundering Acts, and the Financial Intelligent Units. However, their effectiveness in dealing with IFFs remain constrained due to a lack of political will, coupled with political interference in the operations of the institutions established to deal with IFFs, given that politicians may be involved directly or in collaboration with unscrupulous business people to illegally exploit and transfer resources across borders. Furthermore, limited human capacities, low morale, limited budgetary funding, among others, were identified as key factors affecting the operational effectiveness of the various government institutions set up to fight IFFs.

CONCLUSION

In conclusion, the study noted that the problem of IFFs is a global phenomenon that requires joint effort at global level. Curtailing IFFs requires concerted efforts by both developed and developing countries. This, therefore, requires greater emphasis and international cooperation by individual nations on measures aimed at regulating secrecy jurisdictions, strengthening anti-money laundering efforts, enhancing tracking of financial crimes, corruption and enhancing the capacity of the UN Committee of Experts on International Cooperation in Tax Matters, among others. This should be coupled with initiatives in support of transparency in international financial transactions, through the full implementation of such initiatives as UN Resolution 55/188 on the illegal transfer of assets, as well as the Stolen Asset Recovery Initiative.

The arguments for a global approach to IFFs is further strengthened by the fact that only a collective approach to reform the global financial system, can achieve reforms that works for developing countries as well. These measures includes dealing with cases of excessive financial secrecy that allows tax evasion, money laundering, terrorist financing or other criminal activities. This is because many rich nations benefit from financial secrecy or tax avoidance at the expense of a poor country. For instance, where a multinational company headquartered in a developed country, is engaged in transfer mispricing to shift its profits out of a developing country, or where foreign companies use offshore accounts to evade exchange control requirements in developing nations.

In that regard, reforms in the international financial architecture, requiring greater transparency in the banking system could be a giant step towards addressing the problem of IFFs. If banks were obliged to ascertain the identity, source of wealth, and country of origin of their customers and their deposits, this would enhance greater transparency, to the detriment tax havens, which thrives in secrecy. Further, such mechanism will not only discourage IFFs but will also help in the repatriation of stolen assets, as well as enforce compliance with tax laws of respective countries.

Furthermore, global initiative to deal with IFFs needs the full endorsement of developing nations which are often at the receiving end of IFFs. These global measures under the Worldwide Counter-Illicit Financial Flows Initiatives includes, Automatic Exchange of Tax Information, Beneficial Ownership, Country-by-Country Reporting as well as measures to fight Tax, Transfer Pricing, and Profit Shifting.

At country level, countering IFFs would require strengthening of the legal and institutional frameworks that are fit for purpose; credible; enforceable and adaptable to the dynamic and complex illicit activities that facilitate IFFs. Penalties for offenders should be deterrent and incentive compatible. Institutions created to deal with economic crimes, such as the Anti-Corruption Commission and the Ant-Money

Laundering Unit, must be given enough degrees of freedom and autonomy to operate freely without the interference of politicians. Equally important is the need to ensure that the institutions are well resourced and are staffed with well-motivated and technically competent personnel to investigate and deal with complex issues of IFFs.

In mining, there is need to address information asymmetry, regarding the quality and quantity of mineral ores by investing in geological surveys. Such information asymmetry leads to tax avoidance through bad contract negotiation, and illegal exploitation of minerals through underreporting of the quantity and quality of minerals. Further, this should be complemented by reforms in the Mines and Minerals Act, to eliminate discretionary decision making powers and the practice of case-by-case negotiation of royalties and tax concessions for special mining leases, which creates room for corruption. Discretionary powers should be eliminated in favour of a transparent and rule based approach. This can be achieved by introducing standard model contract or enshrining in the law the operational and financial details of the extractive sector that promote national interest. This eliminates room for individual negotiation between Government officials and potential miners.

Furthermore, addressing current constraints of transparency, accountability, and competitive acquisition of mining licences would help deal with the problem of IFFs. Disclosure of information on revenue flows and other benefits obtained from mining, in line with the Extractive Industries Transparency Initiative (EITI), principles, procedures, standards and rules, is also of paramount importance in the fight against IFFs from mining. This could be achieved through reviving the Zimbabwe Mining Revenue Transparency Initiative. Furthermore, the Zimbabwean tax regime needs to be reformed to simplify it by streamlining its multiple components, to balance revenue collections objective and encouraging investment in new exploration and mining, as well as, to take into account the needs small-scale miners.

Zimbabwe's wildlife laws also need refinements to ensure that penalties imposed reflect the true value of the resource being destroyed. Wildlife offences should attract stiffer and rule based penalties that can deter illicit trade in the sector. Equally, the existing framework aimed at addressing illegal logging in Zimbabwe, which is a source of IFFs, tends to focus on low level criminal activity, ignoring the more sophisticated syndicate which may include companies and unscrupulous business people. This requires all the law enforcement agencies to be proactive in the investigation and prosecution of illegal logging and trade of timber.

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