



ILLICIT FINANCIAL FLOWS AND THE RIGHT TO DEVELOPMENT

POLICY BRIEF FOR STATES

Analysed through the lens of the Declaration on the Right to Development, the 2030 Agenda and Sustainable Development Goals and the Addis Ababa Action Agenda, illicit financial flows must be addressed, prevented and controlled, to achieve domestic resource mobilization. Domestic resource mobilization in turn, is key to realizing the right to development and all other human rights, the Sustainable Development Goals, and Financing for Development. National and international policymakers in countries across all stages of development must take concrete steps to address the monumental effects of illicit financial flows on human rights, sustainable development and sustained peace. The Declaration on the Right to Development requires national and international development policies to create conditions favourable to development - an enabling environment for development, human rights as well as peace. The policy guidance which follows is grounded especially in the Right to Development and related human rights norms, standards and principles; SDG Target 16.4 wherein states pledge to significantly reduce illicit financial flows by 2030; SDG target 17.1 which entails strengthening domestic resource mobilization; SDG 10 which aims to reduce inequality within and between countries and SDG 5 aimed at advancing gender equality and women's rights.

While all countries are affected by illicit financial flows in an age of economic and financial globalization, outflows from developing countries are of particular consequence and entail disproportionate impacts given their resource-constrained settings and as a percentage of their public budgets; and longstanding systemic and structural inequalities and vulnerabilities including in the global trade and finance architecture which undermine equality of opportunity for development for all nations and peoples, as required by the Declaration on the Right to Development. The implementation of appropriate national and international policy measures to ensure development and eliminate obstacles to development in line with the Declaration on the Right to Development, mandates states to cooperate on the basis of their sovereign equality, interdependence and mutual interest. Such policy measures would significantly increase transparency in the global financial system, to prevent and regulate illicit financial flows and require the effective channels provided by national, regional and international tax cooperation.

Due to the inherently global and transnational nature of illicit financial flows, the institutional environment for international tax cooperation is of particular significance. In addition to the seminal principle of international cooperation (including shared global responsibilities and mutual accountability, as well as common but differentiated responsibilities), other principles of the Declaration on the Right to Development which apply both locally and globally, include the human rights principles of equality, non-discrimination, participation, accountability and transparency. Relevant Declaration on the Right to Development principles and elements in this context include social justice and equity; free, active and meaningful participation; fair distribution of the benefits of development and fair distribution of income; self-determination and permanent sovereignty over all natural wealth and resources; and equality of opportunity for development for all nations and individuals who make up nations.



AUTOMATIC EXCHANGE OF TAX INFORMATION

RECOMMENDATION 1

States should ensure that all human rights, including the right to development, are respected and promoted in their national tax regulations as well as tax oversight. These should be underscored by the key principles common to all human rights, in particular, participation, transparency and accountability. Given the critical importance of the duty of international cooperation in the Declaration on the Right to Development and its centrality to revitalizing the global partnership and strengthening the means of implementation in the 2030 Agenda and Addis Ababa Action Agenda, states should actively participate in the international efforts on the automatic exchange of tax information, with the objective of preventing the use of offshore tax havens to hide assets and income streams. National customs agencies should treat trade transactions involving a tax haven with the highest level of scrutiny. To this end, states should strengthen the capacity of their customs agencies by equipping and training officers to better detect intentional misinvoicing of trade transactions. Such action would be consonant with the obligations of states under the Declaration on the Right to Development, including to people in other countries who are affected by activities within their territories.

BENEFICIAL OWNERSHIP

RECOMMENDATION 2

Legal requirements should be implemented by states for the public disclosure of the beneficial, or actual, owners of companies in order to address the widespread problem of companies, trusts and foundations that have hidden owners. In order to propel the momentum toward global financial transparency, states should ensure that all enterprises are registered for tax purposes. To avoid unnecessary delays in the registration of companies, relevant state agencies must have adequate capacity to process such registrations. The Financial Action Task Force, an intergovernmental body tasked with the development and promotion of policies to combat money laundering and terrorist financing, has issued two key recommendations to increase the transparency of beneficial ownership of legal persons and of legal arrangements. The Financial Action Task Force recommendations require states to take measures to prevent the misuse of legal persons for money laundering or terrorist financing. The duty of international cooperation and assistance under the Declaration on the Right to Development as well as human rights treaty obligations require such action.

COUNTRY-BY-COUNTRY REPORTING

RECOMMENDATION 3

States should require transnational businesses headquartered in their countries to publish reports of their commercial activities on a country-by-country basis. The transparency on financial and tax information relating to the global allocation of transnational business income and taxes will better ensure that adequate taxes are paid in the jurisdiction where profits are generated. This in turn, will help uphold the human rights principles of transparency and accountability, and constituent principles of the Right to Development, including the duty of states to create an enabling environment for development, fair distribution of the benefits of development and of income, as well as inclusive and equitable development. It would further be consonant with the system of responsibilities envisioned by the Declaration on the Right to Development, of state obligations to people within their jurisdictions, to people in other places who are affected by actions within their territories, and obligations of states acting collectively through international organizations.

INTERNATIONAL COOPERATION

RECOMMENDATION 4

International cooperation is a key principle of the Declaration on the Right to Development. Participation is a key human rights principle, further fortified in the Declaration on the Right to Development principle of free, active and meaningful participation, which would include democratic and inclusive participation, voice and representation for all countries alike in institutions of global governance. International and regional cooperation have the potential to significantly enhance capacity building to redress the systemic problem of illicit financial flows. Under the auspices of the United Nations, international organizations, regional forums and various multi-stakeholder initiatives and efforts, there is a foundation upon which greater political will can be motivated. States already involved in the work of the UN Committee of Experts on International Cooperation in Tax Matters should facilitate the increased representation and participation of lower-income developing countries so that it can act as a global forum for norm-setting on international tax matters. Developed countries that are active in the Organisation for Economic Co-operation and Development's (OECD) Base Erosion and Profit Shifting initiative should call for the participation of developing countries that are not in the OECD's membership. States that are open to the consideration of the creation of an intergovernmental body on tax matters with universal representation under the auspices of the UN should persist in highlighting the potential of such a body in advancing international cooperation for global tax justice.

There are several key UN instruments which establish legal obligations in the field of illicit financial flows. These instruments should be recognized and supported by all states.

The following is a summary of key U.N. instruments that address illicit financial flows:

- United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 1988 (Vienna Convention):¹⁸⁶ This includes provisions on money laundering and international cooperation;
- United Nations Convention against Transnational Organized Crime 2000 (Palermo Convention):¹⁸⁷ This requires states to criminalize money laundering and includes language on extradition, mutual legal assistance and law enforcement cooperation;
- International Convention for the Suppression of the Financing of Terrorism 1999:¹⁸⁸ This requires states to criminalize the financing of terrorism, and adopt powers to freeze and seize funds intended to be used for terrorist activities;
- United Nations Convention against Corruption 2003 (Merida Convention):¹⁸⁹ This requires measures to prevent and criminalize corruption, and provide international cooperation and asset recovery on corruption cases;
- A number of UN Security Council Resolutions¹⁹⁰ have also introduced measures to counter illicit financial flows, in particular by establishing targeted financial sanctions regimes applied to terrorist groups.

REGIONAL COOPERATION

RECOMMENDATION 5

Regional integration arrangements should be used to introduce accepted standards for tax incentives to prevent harmful competition in the effort to attract foreign direct investment. African countries are encouraged to join the African Tax Administration Forum and to provide it with the necessary support, including giving it political standing in African regional processes such as the African Union and Economic Commission for Africa Conference of Ministers of Finance. Developing countries should establish or strengthen independent institutions and governmental agencies responsible for preventing illicit financial flows. These include, but are not limited to, financial intelligence units, anti-fraud agencies, customs and border agencies, revenue agencies, anti-corruption agencies and financial crime agencies. All such agencies should produce regular reports on their activities and findings to national legislatures. They will thereby contribute to creating favourable conditions for international development and human rights as required by the Declaration on the Right to Development, and to transparency, participation and accountability, essential to all human rights. Such steps would help to increase policy coherence in line with both the Declaration on the Right to Development and 2030 Agenda, and are in line with the policy space which all states must have in line with their sovereignty and sovereign equality, explicitly recognized by the Declaration on the Right to Development.

COOPERATION OF INTERNATIONAL ORGANISATION

RECOMMENDATION 6

States should ensure that the international organisations in which they are members, are cooperating and contributing to the international and national efforts in tax cooperation, to prevent and curb illicit financial flows. Coherent tax regimes should be established for the supervision of international organisations by financial supervision agencies. Such regimes should require regular reporting of transactions that may involve illicit financial flows. This would be in line with the shared global responsibilities and mutual accountability of states as members of international organizations, in line with the Declaration on the Right to Development.

VOLUNTARY NATIONAL REVIEWS

RECOMMENDATION 7

As part of the follow-up and review mechanism of the 2030 Agenda and Sustainable Development Goals (SDG), states are encouraged to conduct regular and inclusive reviews of progress at the national and sub-national levels in order to produce a Voluntary National Review. States should use this opportunity among other things, to review how they are addressing SDG Target 16.4 on illicit financial flows and related paragraphs of the Addis Ababa Action Agenda, with a view to realizing the right to development and all human rights; promoting peaceful and inclusive societies, providing access to justice for all and building effective, accountable and inclusive institutions at all levels as per SDG 16; strengthening the means of implementation and revitalizing the global partnership as per SDG 17; and reducing inequalities between and among nations, as well as enhancing gender equality and empowerment, as per SDGs 10 and 5.

HUMAN RIGHTS IMPACT ASSESSMENTS

RECOMMENDATION 8

States should carry out Human Rights Impact Assessments of their tax policies in order to identify and respond to the actual and potential human rights impacts of transnational enterprises. They should ensure that HRIAs include all relevant international human rights norms, standards and principles including those of the Declaration on the Right to Development, and should complement other impact assessments such as environmental or sustainability impact assessments. Human Rights Impact Assessments should be independently verified and include the free, active and meaningful participation of affected communities. If and when negative human rights impacts are found, impact assessments should yield a policy redress where the responsible party is held accountable in a due diligence process appropriate to the legal context of the state.

CAPACITY BUILDING FOR NATIONAL TAX ADMINISTRATIONS

RECOMMENDATION 9

The Declaration on the Right to Development calls for sustained action to promote the rapid development of developing countries, including through effective international co-operation in providing the means and facilities to foster their comprehensive development. Together with SDG 17, Target 17.1, the Addis Ababa Action Agenda and the principle of common but differentiated responsibilities contained in the 2030 Agenda, this calls for capacity building which should be provided for lower-income developing countries that do not yet have tax regulation and oversight, as well as data gathering and processing capacity. Technical assistance and other forms of support should be supported, including through South-South cooperation and meaningful participation in relevant initiatives and programs.

In particular, lower-income countries should be able to employ a fixed transition period in which they receive tax information without a requirement for full reciprocity. Such a grace period would enable their domestic tax authorities to build capacity in order to reap the full benefits of tax information exchanges. In order to curb trade misinvoicing, developed countries should contribute toward the production of a global trade-pricing database that would provide customs agencies access to global average prices of products. Strengthening customs agencies in lower-income developing countries should be facilitated through financial and other forms of assistance.

CONDUCTIVE AND GENDER-SENSITIVE TAX POLICIES AT THE STATE LEVEL

RECOMMENDATION 10

States should promote the prevention and control of illicit financial flows through conducive fiscal and tax policies at the state level. Tax policies should attempt to increase the weight of direct taxes on income and profit capital, while reducing the weight of taxes on low-income communities, and in particular, women in such communities. States should promote tax policies that do not foster tax competition through tax holidays, reductions and subsidies for transnational corporations that are sources of foreign investment. Gender sensitive tax policies should also be prioritised with a view to ensuring that revenue and tax policies are formulated with due consideration to their impacts on women's rights and gender equality.

STATES OF ORIGIN

RECOMMENDATION 11

Regional integration arrangements should be used to introduce accepted standards for tax. States from which illicit financial outflows originate should:

- Have clear laws and regulations that make it illegal to intentionally, incorrectly or inaccurately state the price, quantity, quality or other aspect of trade in goods and services in order to move capital or profits to another jurisdiction or to manipulate, evade or avoid any form of taxation, including customs and excise duties;
- Establish transfer pricing units within their revenue authorities;
- Require their customs officials to use available databases of information about comparable pricing of world trade in goods to analyze imports and exports and identify transactions that require additional scrutiny;
- Review their current and prospective double taxation agreements, particularly those in place with jurisdictions that are significant destinations of illicit financial flows, to ensure that they do not provide opportunities for abuse.

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