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Irene Musselli and Elisabeth Bürgi Bonanomi

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1. Introduction

- 1 Countries have committed to ‘significantly’ reducing ‘illicit financial flows’ (IFFs) by 2030 in accordance with Sustainable Development Goal (SDG) target 16.4. Yet there is still no consensus regarding the concept and definition of IFFs. The dominant narrative, which we deconstruct in Section 2, distinguishes between a ‘narrow’ and a ‘broad’ definition of IFFs (for a review of the debate, see Forstater, 2018a). In a ‘narrow’ sense, IFFs refer to cross-border financial transfers ‘that have a clear connection with illegality’ (World Bank, 2016, 1).¹ The ‘broad’ definition of IFFs stretches the concept further by including transactions that are deemed unethical, even if not illegal in the assessed jurisdiction (High Level Panel on Illicit Financial Flows from Africa, 2015; Independent Expert on the Effects of Foreign Debt, 2016; UNCTAD, 2014).² Making such a clear distinction in relation to tax-motivated IFFs is fraught with serious conceptual problems, as discussed in the following analysis. Beyond the narrow/broad definitional debate, several questions remain with respect to the following (Eriksson, 2017): (1) the type of cross-border transfers that qualify as IFFs—whether money flows or anything with monetary value, from loans embedded in private contracts to smuggled physical goods; (2) the type and degree of illegality involved; and (3) whether the source, the

use, or the transfer mechanism of a cross-border transfer should be assessed as illegal. The debates point to major divergences and disagreement on all these points. In the end, the definition of IFFs remains clouded in ‘open questions, uncertainties, and inconsistencies’ (Eriksson, 2017). On the one hand, this definitional uncertainty has served, and still serves, the ‘IFF agenda’. Looking back, it has been instrumental in building political momentum around the IFF issue. Building that momentum required emphasis on aggregates, and postponement of technical disagreements about the specifics of the issue at stake. Looking forward, this definitional ‘openness’ ensures some built-in flexibility in the IFF debate, which is adaptable to the fast pace of legal reform, and to changes in underlying policy perceptions. On the other hand, lack of clarity and agreement about what constitutes IFFs can give rise to misunderstandings and policy disagreement. It is a stumbling block to any effort to rigorously gauge the magnitude of IFFs. Further, it hinders the design of effective policy responses to curb IFFs, since regulatory responses require clarity as regards targeted actors, techniques, and motives for IFFs.

- 2 Against this background, this article reviews and challenges some key tenets of the IFF debate, and articulates some lines of legal reasoning that can help to define the boundaries of what constitutes illicit flows (or not). It does so with reference to three hotly contested areas in the debate: the *legal/illegal distinction* in relation to tax-motivated IFFs; the *tension between ‘development’ and legal approaches to IFFs*; and *how to reconcile aggregate and disaggregate approaches* under the IFF agenda. In each of these areas, the analysis briefly rehearses the state of the debate, challenges some entrenched assumptions, and presents ideas that help to reconcile conflicting views. It concludes with some summary observations.

2. Tax-Motivated IFFs: Moving Beyond a Polarised Debate

- 3 It is customary in the literature and in policy debates to distinguish between a ‘narrow’ and a ‘broad’ definition of IFFs (for a review, see Forstater, 2018a, 4–7). The former requires a breach of the law (‘illegal’ activities). The latter encompasses unethical acts that are deemed to be formally lawful, if unregulated (‘illicit’ activities). This distinction has gained wide acceptance in the debate on tax-motivated IFFs, with different outcomes. Proponents of the ‘narrow’ definition argue that transfers associated with tax *evasion* (illegal) qualify as IFFs, while tax *avoidance* schemes (formally compliant with ‘the letter of law’) do not, even if unethical (World Bank 2016, 2; Forstater, 2018a; 2018b). Advocates of the ‘broad’ approach argue that avoidance practices may still fall under a ‘broad’ definition of IFFs that includes unethical (though allegedly lawful) practices (High Level Panel on Illicit Financial Flows from Africa, 2015; Independent Expert on the Effects of Foreign Debt, 2016; UNCTAD, 2014).
- 4 While the narrow/broad distinction is conceptually appealing,³ it is, to a significant extent, misleading. In real life, it is hard to draw a line between ‘illegal’ and ‘illicit’ activities: as discussed below, so-called illicit activities often involve illegal elements. This is particularly so in the area of tax avoidance: the legal assessment of tax avoidance practices is a circumstantial process of interpretation and constant adjustment, in a dynamic and adaptive regulatory environment. This line of reasoning is detailed below. The proceeding analysis first clarifies the use of key terms—tax

evasion and avoidance. It then critically reappraises the analytical distinction between ‘illegal’ and ‘illicit’ with regard to tax evasion and avoidance practices. Finally, it seeks to advance beyond that distinction by endorsing a definition of tax-motivated IFFs that, while anchored in law, is dynamic and adaptive to policy changes, and levels the playing field between countries with different lawmaking and law-enforcement capacities.

2.1 Tax Evasion and Tax Avoidance

- 5 For analytical purposes, it is useful to retain some legally relevant terms and concepts from the perspective under critique. In line with the dominant framing of the debate, the terms ‘tax evasion’ and ‘tax avoidance’ are here used to denote different tax behaviours.⁴ UK Treasury Minister Gauke drew the following distinction during a parliamentary debate in 2010—a distinction upheld in the UK 2015 government paper on tax avoidance (HM Treasury, 2015):
- 6 *Tax evasion* occurs when people or businesses deliberately do not pay the taxes that they legally owe. They can do so by underreporting income, over-reporting expenses, or simply not paying taxes owed. Tax evasion encompasses the ‘hidden economy’ in which ‘people conceal their presence or taxable sources of income’ (HM Treasury 2015, 5).
- 7 *Tax avoidance* involves ‘bending the rules of the tax system to gain a tax advantage that Parliament never intended’ (HM Treasury 2015, 5). It results in ‘compliance with the letter but not the spirit of the law’ (HC Deb 12 July 2010 c706, reported in Seely, 2018). Tax avoidance practices typically entail ‘taking advantage of the technicalities of a tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability’ (European Commission, 2012). This type of avoidance typically involves highly artificial and contrived arrangements whose sole or main purpose is to reduce or eliminate tax liability.⁵ The practice is sometimes referred to as ‘aggressive tax planning’ (European Commission, 2012; 2015; 2017), or ‘abusive’/‘aggressive tax avoidance’ in order to distinguish it from so-called legitimate tax planning. At the global level, it substantially overlaps with ‘base erosion and profit shifting’ (BEPS) under the G20/OECD BEPS programme.
- 8 While this taxonomy brings some theoretical clarity to the debate, it is important to acknowledge that the boundaries between tax avoidance and tax evasion remain blurred in day-to-day reality. In practice, there is a ‘continuum of tax aggressiveness’ from tax avoidance to outright tax evasion (European Commission, 2017, 23; Hearson 2014, 7), and much depends on the circumstances of the case. Legal assessment of avoidance practices is seldom simple or obvious, as discussed below.

2.2 Tax Avoidance: Illegal or Illicit?

- 9 As defined above, tax evasion directly breaches the law. Tax avoidance exploits tax loopholes and mismatches to circumvent a tax law without directly violating the ‘letter of the law’. Building on this definition, some consider avoidance practices outside the scope of IFFs, lacking in their view a clear connection with illegality (World Bank, 2016, 2; Forstater, 2018a; 2018b); others argue that avoidance practices still fall within a broad definition of IFFs that encompasses commercial practices perceived as unethical,

even if legal—termed ‘illicit’ practices (High Level Panel on Illicit Financial Flows from Africa, 2015; Independent Expert on the Effects of Foreign Debt, 2016; UNCTAD 2014). This view resonates with basic notions of law *versus* justice, and is widely upheld by economists and commentators (for a review, see Mehrotra, 2018).

- 10 The distinction between illegal and illicit tax behaviour, and between ‘narrow’ and ‘broad’ definitions of IFFs, is well established and intuitively appealing. Yet it is problematic since it mis-characterises the legal terrain by unduly restricting the legal sphere and the legal process of interpretation. It can be criticised on several grounds.
- 11 First, as extensively elaborated by Picciotto (2018; 2018b), legal assessment of tax avoidance practices is a matter of interpretation. This points to some ‘indeterminacy in rules’ and to ‘the scope within law to legitimise contradictory decisions’ (McBarnet and Whelan, 1991, 852-53).⁶ Note in this respect that tax rules often embed commercial concepts that require fact-intensive assessment of underlying business structures. Determining whether a corporate tax position is correct is generally a complex, context-specific endeavour, requiring a number of judgment calls by the taxpayer, the tax administration, and eventually the court if the matter is litigated. In some respects, it is only the legal challenge that determines if the tax filing position is correct (Quentin, 2017; Devereux et al., 2012). Note also that several tax provisions are in the form of circumstantial, open-ended standards that call for a balancing of multiple factors to determine whether a position is illegal, requiring principled decisions and purposive interpretation. Ultimately, it is incumbent on the revenue authority or the court to authoritatively categorise the facts to place them under a particular legal classification.
- 12 It is important to note that this interpretative process is not value-free: when interpreting a specific law provision, judges typically seek to determine the ‘intention’ of legislation, viewing legal terms in light of the objectives and rationale of the law. By interpreting the law purposively, a court may strike down an arrangement that follows the letter of the law, but violates its intention. Judges use different approaches and techniques to do so. Depending on the legal system in place in a given country, these techniques include statutory interpretation and construction, judicial anti-abuse doctrines, and anti-abuse theories of law.⁷ This process of legal interpretation *per se* problematises distinctions between the ‘letter’ and ‘spirit’ of the law, on which the illegal/illicit distinction largely rests (see also Harmon et al., 2015; McBarnet and Whelan, 1991; Minto, 2016).⁸
- 13 Second, in tax matters, the reach of the law has markedly extended into tax avoidance areas. As a consequence, the distinction between tax evasion (illegal) and tax avoidance (formerly perceived as legal) is blurring somewhat. This reflects the increased pace and breadth of regulatory reform in tax law over the past years—under the BEPS agenda, in particular. Two major developments are worth noting in this respect: the enactment of specifically targeted anti-avoidance legislation, and the introduction of *general anti-abuse rules* (GAAR). Many jurisdictions have introduced specifically targeted laws to close regulatory loopholes and redress mismatches that provided opportunities for regulatory arbitrage and abuse; these include transfer-pricing rules, interest deductibility rules, thin capitalisation rules, controlled foreign company rules, and anti-hybrid rules, as well as ‘switch-over’ rules designed to prevent ‘double non-taxation’ of certain dividends, capital gains, and profits.⁹ These rules defeat the most common methods used by companies to aggressively avoid taxes, including through

artificial schemes that shift income offshore through interest payments, royalty payments, and strategic transfer pricing. Going a step further, many countries have enacted so-called ‘catch-all’ rules, typically in the form of GAARs that rule out transactions designed to avoid tax.¹⁰ A GAAR is a ‘provision of last resort’ that can be invoked by a tax authority ‘to strike down unacceptable tax avoidance practices that would otherwise comply with the terms and statutory interpretation of the ordinary tax law’ (Waerzeggers and Hillier, 2016, 1). GAARs are meant to ‘strike down those otherwise lawful practices that are found to be carried out in a manner which undermines the intention of the tax law’ (ibid.). All tax arrangements that satisfy the relevant provisions of a given tax code yet simultaneously undermine its intention are potential targets for GAARS—thus, possibly making them unlawful. This per se problematises the statement that tax avoidance is legal. Certainly, businesses will adjust and find new, more subtle forms of elusion. Targeted anti-avoidance legislation can actually create avoidance opportunities through new loopholes and mismatches, absent a general anti-abuse rule. Absent ‘catch-all’ GAAR-type rules, the regulation of tax avoidance typically engenders a ‘balloon effect’: regulators squeeze the balloon in one place only to see it inflate elsewhere. But the law will seek to adapt, resembling a cat-and-mouse game of constant pursuit, near captures, and repeated escapes.

- 14 Third, it is important to stress that ‘illegality’ is a complex concept that must be assessed in the context of complex, multi-layered legal settings. Public discourses tend to conflate illegality and criminality. According to this logic, tax avoidance is legal, since normally it is not a crime, and thus should not invite legal sanctions. This line of reasoning is problematic, however. The notion of ‘illegality’ not only embraces actions contravening criminal law, but also violations of civil or administrative law. To put it clearly, some actions may be unlawful even if they are not criminal. Take the example of aggressive tax optimisation schemes: in the mainstream public discourse, these practices are deemed formally legal. Yet, as discussed above, under some circumstances the tax authority has the right to challenge the tax arrangement and deny the tax advantage that an ‘abusive’ scheme would otherwise enable. In this case, tax avoidance does not amount to a criminal tax offense. At worst, it may expose the party in question to civil penalties. Yet the counteracted scheme can be said to be unlawful in administrative terms, to the extent that the tax authority has the regulatory power to strike it down. It is also important to stress that ‘criminal’ is, per se, a multi-layered and nuanced concept: most jurisdictions provide for different classifications of criminal offenses—for example, crime, *délit*, and contravention in civil law countries,¹¹ or felony and misdemeanour in Anglo-American law. To sum up, what is commonly presented as legal or ‘quasi-legal’ is often technically unlawful, even if the conduct only amounts to an infraction not liable to a prison sentence.
- 15 Finally, the mainstream public discourse tends to mix up two questions that should be kept conceptually distinct: the question of legality in theory, and that of whether the existing law is being *properly applied and enforced*. As discussed, in many cases tax avoidance may be unlawful in contexts where tax law has attained a certain level of sophistication. Nevertheless, many cases go undetected and are never brought before a court. Further, when a case is litigated, there may be a degree of judgment involved in assessing what activities are ‘abusive’ or not, creating uncertainty about the outcome of litigation.¹² Note also that there can be many delays before a case is finally litigated, and decisions are often weakly enforced. In these circumstances, many avoidance schemes succeed ‘by default’ in the sense that they are simply not litigated or are

drawn out indefinitely (Quentin, 2017). For this reason, businesses may deliberately choose risky tax positions if they have a perceived likelihood of success. This explains the mass-marketing in the UK of avoidance schemes with as little as a 50 per cent chance of success if challenged in court (House of Commons Committee of Public Accounts, 2013).¹³ This risk appetite accounts for the persistent ‘tax gap’ between tax collected and due (Seely, 2018),¹⁴ not only in countries with weak governance systems, but also in countries with well-developed legal systems.

- 16 These examples highlight the need to reconsider simplified ‘illegal’ *versus* ‘illicit’ distinctions (and tax ‘evasion’ *versus* tax ‘avoidance’ distinctions) in the IFF debate. The question of what is legal, and what is not, ‘is a set of grey areas with many nuances and disagreements’ (Shaxson, 2019). In the end, it is hard to draw a line *ex ante*¹⁵ between tax evasion and tax avoidance, or between avoidance activities that are unlawful or legal: the legal assessment of tax avoidance practices is a circumstantial process of interpretation and constant adjustment, in a dynamic and adaptive regulatory environment.
- 17 Two observations follow from the above.
- 18 First, what is genuinely at stake, today, is not the illegal *versus* illicit dilemma, but uncertainty over the *ex-ante* legal characterisation of tax arrangements. As previously discussed, the pace of regulatory reform in tax law has accelerated over the past decade. In a fast-moving regulatory environment, what was lawful yesterday may be unlawful today, and legality is, increasingly, a matter of judicial and administrative interpretation. The shift in tax law from detailed legal drafting towards broad purposive directives such as general anti-abuse rules may possibly exacerbate this feature of the legal system. GAARs are inherently vague and purposive, afford decision makers more discretion than detailed rules, and may generate some uncertainty about the tax treatment of business transactions.¹⁶
- 19 Second, the focus on the illegal *versus* illicit distinction may conceal something else of critical import: capacity gaps regarding tax administration and prosecution, particularly in resource-strained jurisdictions. These gaps may lead to lack of regulation or weak legal enforcement. A narrow definition of tax-motivated IFFs that only considers the positive law applied in the assessed jurisdiction fails to consider the variability of administrative and enforcement capacity across countries. As a result, it neglects IFFs in countries with lower tax administration capacity, lower prosecution capacity, and less sophisticated legal systems (Chowla and Falcao, 2016).

2.3 Moving beyond ‘Illegal’ *versus* ‘Illicit’: Evolving Legal Norms and Principles

- 20 These considerations show the need to move beyond simplified distinctions (illegal *versus* illicit) that fail to bring clarity to the debate. How, then, to move forward? A pragmatic way out is to reconstruct the ‘broad’ definition of IFFs in a way that anchors that definition to legal concepts and constructs, as described in the following.
- 21 On the one hand, the definition of IFFs should be anchored in legal concepts, rather than ethics, in order to avoid unproductive subjective arguments over moral values. It is thus important to define the boundaries of what constitutes illicit flows according to concrete legal understandings, making reference to legal rules and legal constructs.

- 22 On the other hand, the corresponding legal assessment of IFFs should be broad. First, it should move beyond ‘bright line’ rules and also encompass legal standards and doctrines that set the terms for the legal assessment. As further discussed in Section 3.2.1, bright-line rules are clearly defined rules about what is permissible or not, leaving little room for varying interpretation; standards are imprecise and circumstantial and require determination of the legal outcome based on principled decisions.¹⁷ Both are enforceable parts of the positive law of the State. Reference to standards means emphasising commonly shared anti-abuse principles that can be found across domestic legal systems. These principles can be considered the legal benchmark against which to define the contours of what constitutes IFFs for reasons of policy analysis, even in those countries where avoidance arrangements are not regulated.¹⁸ Note that while (bright-line) rules are ‘precise and ex ante in nature’ (Casey and Niblett, 2017, 1407), standards are ‘circumstantial and open-ended’, requiring determination of the law’s content only ex post, once the judge has made a fact-specific determination (Parisi, 2004, 510).¹⁹ Second, the legal assessment should not be confined to the positive law in force in the assessed jurisdiction: it should comparatively refer to major legal developments in other jurisdictions. There might be (rare) cases where the legal system in question is so rudimentary that it does not integrate any anti-abuse rule or principle at all, leaving avoidance practices unregulated. Yet aggressive avoidance practices still go against rules and standards established across most jurisdictions. For policy purposes, the legal definition of IFFs should refer to these widely recognised rules and norms. It is important to note, in this respect, that IFFs involve cross-border transfers that straddle jurisdictions. Their legality is to be assessed with respect to the laws of different countries—transit, home and host countries. Furthermore, as discussed in the following section, the legal assessment may also take into account rules and principles of public international law, including human rights law. As discussed in Section 3.2.1, reference to public international law may further expand the legal terrain, extending to practices that currently stand at the periphery of the IFF debate.
- 23 Along these lines, for definitional purposes, ‘illegality’ should be flexibly interpreted with reference to national or international law *and evolving anti-abuse standards*, with a view to reflecting the dynamic, evolving nature of legal processes. In tax matters, this implies considering the wealth of legal principles and statutory enactments that collectively challenge the widely held assumption that tax avoidance is legal while tax evasion is not. The previous analysis has drawn attention to lines of judicial reasoning, judicial doctrines, and statutory enactments aimed at countering abuse of law and tax avoidance. Based on this wealth of legal material, it is possible to identify general principles that are crucial to the assessment of tax-motivated IFFs. In particular, GAAR provisions reject the idea that taxpayers are free to use their ingenuity to reduce their tax bills by any lawful means. Instead, they stipulate that abuse or misuse of tax laws is not a lawful course of action. Some GAARs also seek to establish the ‘substance over form’ doctrine in tax law. A key reference norm is that of realigning taxation with economic substance and value creation. That is also the stated aim of the BEPS programme. Interestingly, this overriding BEPS principle echoes the legal doctrines of ‘economic substance’ and ‘substance over form’ that have long been a part of the tax law of many countries.²⁰ In some respects, soft law legal instruments are integrating long-standing anti-abuse principles into the ‘mainstream’ policy discourse. In turn, these principles set norms that inform lawmaking. Such construction of ‘illegality’

(and IFFs) tends to blur the distinction between soft and hard law. Most importantly, by referring to international standards and principles of law, it levels the playing field between countries with different regulatory and law enforcement capacity to seize and sanction tax avoidance.

- 24 Questions remain as to whether and how such definition of IFFs, anchored in legal concepts, can be reconciled with a ‘development’ perspective on IFFs, which goes beyond the legal characterisation of activities. This matter is discussed below.

3. Development and Legal Perspectives on IFFs: Bridging the Gap

- 25 A further perspective is relevant to efforts to determine what constitutes IFFs. In order to resolve the narrow/broad controversy, some observers argue for adopting a functional, purposive interpretation of IFFs. They move beyond the question ‘*What are we measuring?*’, and instead emphasise the question ‘*Why are we measuring?*’, so as to redirect attention to revenue (or, broadly, development) impacts of relevant income/wealth transfers, and away from narrow discussion of the strict illegality (or not) of such transfers. The following analysis briefly sketches the main tenets of this ‘development approach’ to IFFs. It then seeks to ‘translate’ some key insights from that approach into legal terms.

3.1 A ‘Development Approach’ to IFFs

- 26 Under a ‘development approach’ to IFFs, the key issue in defining IFFs is the revenue impact of the flows. More broadly, the key underlying concern is that of ‘the impact of illicit financial flows [...] on the economic, social and political stability and development of societies’ (UN General Assembly, 2016, 1). Pursuant to this approach, IFFs are defined as international financial flows that have a negative net impact on sustainable development, when all their direct and indirect effects are taken into account (Blankenburg and Khan, 2012; Miyandazi and Ronceray, 2018). This definitional approach focuses on the revenue (or, broadly, the development) impact of transfers, rather than merely on the illegality of transfers. Its central question is that of whether, or to what extent, financial flows damage the development of poorer countries, irrespective of whether the flows are legal, illegal, or fall in a grey area.
- 27 The ‘development impact’ approach has two key corollaries.
- 28 On the one hand, a development-focused definition of IFFs potentially encompasses transactions that, although *prima facie* lawful (until proven unlawful), may have adverse revenue impacts on developing countries. The reach of the IFF agenda would expand to include such issues as business tax incentives, price unfairness, and the allocation of taxing rights under double-tax agreements.²¹ These arrangements may erode developing countries’ tax base and result in significant revenue loss. For example, it has been estimated that US tax treaties cost their developing-country treaty counterparts at least USD 1.7 billion in revenue every year (de Mooij et al., 2015, at 185). Under a ‘development approach’ to IFFs, these outflows constitute IFFs, irrespective of their legal characterisation. This approach resonates with the broad IFF agenda pushed by the pan-African institutions working on IFFs in Africa.²²

- 29 On the other hand, the development definition of IFFs excludes flows that, although in breach of some laws, have no negative net impacts on sustainable development (Miyandazi and Ronceray, 2018). It has been observed, in this respect, that rule-violating transactions are not all equally harmful (Blankenburg and Khan, 2012; OECD, 2018). For example, informal value transfers are especially important in countries where the formal banking system is too expensive for the poor. Transactions conducted through these informal systems of money transfer do not fit under a development definition of IFFs, even if illegal under domestic law (Eriksson, 2017). Similarly, unreported artisanal mining may feature a high degree of subsistence-level criminal activity: it provides income for people lacking credible alternative livelihoods, and the profits may be reinvested in the local economy (OECD, 2018). One step further, some authors argue that corruption-related IFFs also require nuanced distinctions. They observe that, for example, bribes meant to bypass unproductive red tape may enable economic activities, even if they undermine the rule of law (Miyandazi and Ronceray, 2018; see also Khan and Andreoni, 2018). In specific cases, some scholars acknowledge, it is also possible to identify exceptions to the general harmful nature of tax abuses: for example, profit shifting to avoid illegitimate expropriation by a predatory regime in a fragile state may undermine the tax base, but also make investment viable (Blankenburg and Khan, 2012; Khan and Andreoni, 2018; Miyandazi and Ronceray, 2018). Overall, the point is made that IFFs may be driven by ‘inappropriate or contradictory formal rules, or low capabilities of firms in developing countries’ (Khan and Andreoni, 2018). IFFs thus reflect structural drivers that cannot be changed in the short-to-medium term without hurting the local economy or social set-up. Tackling or diminishing these flows could prove difficult and the development impact may be negative in the short to mid-term.
- 30 The ‘development approach’ contributes a useful policy orientation to the debate by drawing a distinguishing line between harmful and non-harmful patterns of conduct under the IFF agenda. Yet it blurs the connection with illegality, raising the question of how to reconcile ‘development’ and ‘legal’ perspectives on IFFs. It is important to tackle this question and establish ways to bridge between legal constructs and development perspectives, as discussed below.

3.2 Legal ‘Translations’

- 31 In order to reconcile development and legal views of IFFs, it is useful to explore how to translate some of the insights from the ‘development approach’ into legal terms. The objective is to enrich the legal debate on IFFs, while keeping the definition of IFFs firmly anchored to legal concepts.
- 32 Overall, the development approach encourages moving beyond formalistic, static conceptions of IFFs and towards more purposive interpretations, linking IFFs to efforts to mobilise domestic resources for development. More precisely, it firmly embeds the IFF agenda in the ‘sustainable development’ agenda, in particular to the 2030 Agenda for Sustainable Development and the SDGs²³ as well as the Addis Ababa Action Agenda (AAAA).²⁴ These agendas explicitly anchor IFFs in domestic resource-mobilisation efforts. The political commitments enshrined in the 2030 Agenda and the AAAA are legally significant as ‘soft law’. For example, they assist in interpreting existing treaty

rules and contribute to the gradual formation of new rules through the political lawmaking process.²⁵

- 33 Such embedding of the IFF debate in the sustainable development framework has concrete legal implications, in at least two respects. First, it implies some *shift from clearly defined ('bright line') rules to standards, and from categorisation to complex balancing tests* (Section 3.2.1). Second, it leads to a focus on *outcome and impact assessments* that go beyond legal formalisms (Section 3.2.2). These developments and their concrete implications are discussed below with specific reference to IFFs.

3.2.1 From 'Bright Line' Rules to Complex Balancing Tests

- 34 What does a shift from bright-line rules (categorisation) to standards (balancing tests) mean, and how does it apply to the legal assessment of what counts as IFFs? As mentioned, bright-line rules are clearly defined rules about what is permissible or not, leaving little room for varying interpretation. Standards are imprecise and open-textured and require determination of the legal outcome based on principled decisions. In practice, legal systems are likely to combine both (McBarnet and Whelan, 1991, 852). The rules/standards distinction echoes the distinction between legal 'categorization' and 'balancing': categorisation is rule-like, while balancing corresponds to standards (Sullivan, 1992, 59). More precisely, categorisation is 'taxonomic': it sets bright-line boundaries and classifies facts as falling on one side or the other (Sullivan, 1992, 59). Balancing tests, by contrast, require weighing and balancing multiple factors in a legal case, and the legal outcome depends on how the judge balances competing normative interests. Open-textured standards and balancing invite 'particularisation' in the application of the law, allowing exceptions to be made when individual circumstances appear to call for them.²⁶ Further, they call for 'systemic law interpretation and systemic lawmaking' (Bürge Bonanomi, 2015b, 29; 2015a). 'Systemic law interpretation' implies open-textured rules interpreted systematically by reference to other legal regimes relevant in the context (*ibid.*). Systemic lawmaking requires 'lawmaking procedures that are shaped by the "duty to include", the "duty to structure and weigh", and the "duty to develop optimal options"' (Bürge Bonanomi, 2015b, 29).²⁷ The quest is for regulatory coherence and convergence, beyond legal fragmentation (Bürge Bonanomi 2015b, 29–30; Cottier et al., 2011).
- 35 With specific reference to IFFs, the balancing of competing rights or interests may lead to authorising otherwise unlawful conduct. It leads to qualifying and/or narrowing the scope of IFFs, with an eye to the underlying factual circumstances or competing policies at stake. Complex balancing tests have already begun informing legal assessments of what counts as 'illegal'. This may be seen regarding rule-violating activities that provide income for people that lack credible alternative livelihoods—for example, illegal harvesting, unrecorded artisanal mining, informal cross-border trade, and informal value transfers. In the judicial assessment of these practices, the need to satisfy basic needs may be considered an attenuating circumstance that lessens the severity of a crime and results in reduced charges. Assessment may entail 'criminal law defences of necessity or duress', whereby external constraints that compel a defendant to transgress the law 'lessen or extinguish culpability' (Gilman, 2013, 498; Law Reform Commission, 2006). Going further, the 'right to life' may be asserted, for example, to justify poaching or illegal resource extraction (and associated trade) by impoverished peasants in contexts of extreme duress. Indeed, from a human rights perspective,

access to the basic conditions necessary to sustain life is a human right.²⁸ It translates into the ‘right to life’, inextricably linked to the right to food, as protected by international and regional treaties, customary international law, and domestic legal systems. Balancing is here a matter of enforcing domestic laws in ways that do not compromise the human rights obligations of states.²⁹

36 The balancing of competing rights and interests may also serve to expand the legal scope of IFFs beyond its current reach. As regards tax-motivated IFFs, sustainability concerns encourage examination of adverse ‘spillover effects’ of a country’s tax regime on other countries. Spillovers refer to ‘the impact that one jurisdiction’s tax rules or practices has [sic] on others’ (IMF, 2014, 12). Concerns arise, in particular, when jurisdictions with attractive tax regimes divert taxable income from other countries, affecting the ability of tax administrations in more fragile states to raise revenue needed for sustainable development. Translated into legal terms, the tax spillover debate requires the weighing of competing rights and obligations under international law. On the one hand, under deeply entrenched fiscal sovereignty principles, states are free to tax corporations as they wish—this is a matter of domestic concern. On the other, states have extraterritorial obligations in the area of economic, social and cultural rights (ETO Consortium, 2013). In particular, countries whose internal tax policies have adverse livelihood impacts on other countries may stand in breach of their duty of international cooperation and assistance (for a review, see Lusiani and Cosgrove, 2017).³⁰ Under human rights law, unaddressed tax spillovers may breach governments’ obligations to refrain from conduct that impairs the enjoyment of human rights abroad (International Bar Association, 2013; Lusiani and Cosgrove, 2017). It would also be interesting to consider the possible legal outcomes of transposing the ‘no harm’ international law principle from environmental spillovers to tax spillovers.³¹ As of today, the balance has been struck in favour of the tax sovereignty of the enacting state: in the dominant policy discourse, financial flows driven by tax competition and legitimate tax-planning schemes do not count as illicit, whatever their development impacts, since tax rates and incentives are largely perceived as a matter of fiscal sovereignty. It remains possible that the balance may tilt towards an equitability focus, driven by sustainability concerns, in the future.³² Much depends on the legal weight that decision makers and judges give to international human rights obligations, particularly with respect to economic, social and cultural rights.

37 To sum up, embedding the IFF debate in the sustainable development framework increases the need to weigh and balance multiple factors when assessing what counts as illicit flows. The integration of sustainability concerns into the legal definition of IFFs encourages evaluation of socio-economic circumstances that may excuse otherwise wrongful conduct—‘particularisation’ in the application of the law. Further, it calls for ‘systemic’ interpretation and ‘systemic’ lawmaking, making reference to other relevant legal regimes, for example by importing human rights claims into tax law.

3.2.2 From Form to Substance

38 Going further, integration of sustainability concerns into domestic and international law—and the related shift from rules to standards, and from categorisation to balancing—has ramifications for the type of legal reasoning involved. It calls for a less formalist, technically oriented conception of the law, and instead favours more ‘substantive’ legal

reasoning. ‘Legal formalism’ ‘insulates the law from other social fields; it structures the law according to standards of “analytical conceptuality, deductive stringency, and rule-oriented reasoning”’.³³ A more substantive style of legal reasoning places more emphasis on the ends pursued by lawmakers and on ‘the substantive justice of the outcome’ (Craig, 1997, 6).³⁴

- 39 This change is more profound than it may first appear. It leads to assessing the legality of a course of action in light of the fairness of its outcomes. It requires ‘policy instruments for integrative lawmaking’, such as ‘sustainability impact assessments’ (Bürge Bonanomi, 2015b, 30). It also ‘modulates’ regulatory responses on the basis of varying socio-economic conditions, for example by specifying impact thresholds that trigger a state’s responsibility (Musselli, 2017). Under this approach, international tax rules should take into account distributive dynamics and outcomes in determining what constitutes unlawful cross-border transfers, to some extent collapsing legal assessments into social and economic impact assessments. Such an approach goes some way to bridging legal and economic understandings of IFFs, favouring a broad and pragmatic treatment of IFF problematics, as discussed below.

4. Unpacking the IFF Agenda? A Pragmatic Approach

- 40 Maintaining a broad definition of IFFs anchored in law ultimately requires taking a pragmatic approach when it comes to corresponding measurement of IFFs, research, and policy making. The key question, addressed below, is how to ‘unpack’ the resulting IFF work programme, without unravelling the whole IFF agenda.

4.1 Unpacking versus Broad Definition

- 41 Some observers question the policy relevance of an all-inclusive IFF agenda (see for example Reuter, 2017). They recommend breaking down IFFs into discrete categories and treating them separately, rather than developing an agenda that treats them as a single phenomenon. For advocacy purposes, they argue, it has been useful to aggregate bribery, tax evasion, corporate profit-shifting, currency regulation evasion, criminal enterprises and earnings, etc. under a single umbrella. However, for policy and research purposes, it is better to disaggregate.
- 42 Indeed, there is a need to add ‘granularity’ to the analysis of IFFs, since emphasis on aggregates tends to conceal key differences in terms of underlying economic and legal dimensions. It is important to disentangle the various dimensions of the phenomenon and isolate key variables, including: (1) the *sources of the proceeds*—whether bribes, tax evasion or avoidance, corruption, currency regulation evasion, sanctions busting or earnings from criminal enterprises; (2) the *various actors involved*—corporate groups or physical persons, public officials or private persons; (3) the different *push and pull drivers* that motivate IFFs, including tax differentials, currency controls, or secrecy provisions; (4) the *geography of IFFs*, from source to recipient countries through transit countries; and (5) the *channels* through which illicit funds flow, ranging from simple smuggling to elaborate trade-based money laundering techniques. A circumstantial assessment of these facts is needed to appreciate the governance challenges involved in trying to curb IFFs.

- 43 At the same time, the broader notion of IFFs remains useful for policy and research purposes, leaving aside advocacy aims. There are at least three sets of arguments that can be made for a broad IFF agenda. First, a single IFF agenda helps to improve regulatory coordination, between and within countries, across a spectrum of interventions. An agenda that treats IFFs as a single phenomenon encourages moving forward in a synchronised manner on multiple fronts. It counters the tendency, inherent in legal specialism, towards fragmentation and duplication. Government actions to tackle the components of IFFs require coordinated responses across different administrations, including revenue authorities, banking supervisors, financial intelligence units, customs agencies, and law-enforcement agencies. An integrated agenda highlights the operational interconnectedness of different specialist areas of law that tend to operate in silos: money laundering and banking prudential requirements, anti-bribery laws, customs law and enforcement, reporting and due diligence requirements, including professional standards for corporate service providers, and multiple exchange of information and transparency requirements.³⁵ This holistic approach is necessary to properly address avoidance practices pursued by businesses: specifically targeted interventions will just spur new schemes to circumvent them (the ‘balloon effect’); an integrated package of coordinated policy interventions could eventually burst the balloon.
- 44 Second, IFFs differ, but they tend to use similar techniques and facilities: abusive offshore structures and devices, secrecy systems, and a host of facilitators, including the legal profession (Cobham and Janský, 2017; Picciotto, 2018a; 2018b). A single IFF agenda can converge and heighten regulatory attention on these ‘nerve centres’ of the IFF architecture. Regulatory efforts directed at these hotspots would likely have multiplier effects across the whole spectrum of IFFs, since offshore structures, secrecy jurisdictions, and facilitators cater to different IFFs simultaneously: they are used to conceal or launder the proceeds of corruption or earnings from criminal enterprises, and they facilitate tax avoidance schemes (Picciotto, 2018a; 2018b).
- 45 Third, the IFF agenda informs other discourses, leading to cross-fertilisation and mutual reinforcement of public narratives and work programmes. For example, there are ‘distinct areas of direct overlap’ between the Domestic Resource Mobilization (DRM) agenda and the IFF agenda (World Bank, 2017). Further, the IFF agenda serves to inform and deepen the emerging debate on Sustainable Finance (SSF). Overall, DRM and IFFs, as well as SSF and IFFs, are interlinked at critical junctures in current development discourses. These different strands of work can work together to support comprehensive reform strategies. Cutting off one part of the discourse would weaken the whole fabric.
- 46 These considerations encourage use of a broad, but pragmatic agenda, as discussed below.

4.2 A Broad, but Pragmatic Agenda

- 47 The arguments outlined above highlight the usefulness of maintaining a broad, flexible definition of IFFs, within a unified agenda. This brings us back to the initial question: how can we add ‘granularity’ and operational significance to the IFF work programme, without unravelling the whole IFF agenda? The recommended strategy is that of keeping a broad, flexible definition of IFFs, and customising it as needed for specific

analytical or policy purposes (Section 4.2.1). At the same time, the need for a pragmatic approach necessitates breaking down the IFF agenda into workable modules and corresponding indicators (Section 4.2.2).

4.2.1 A Broad Definition of IFFs, but Anchored in Law

- 48 As discussed earlier, the definition of IFFs must be anchored in law, rather than (solely) ethics, in order to establish more precise, objective contours regarding what counts as ‘illicit flows’. Accordingly, IFFs should explicitly refer to cross-border transfers of money or assets *connected with some illegal activity*. Yet, as discussed, illegality should be broadly interpreted. First, legal assessment should extend to legal standards and doctrines, going beyond bright-line rules. Further, it should not be confined to the positive law in force in the assessed jurisdiction; it should also refer to rules and legal principles that have attracted wide international recognition. Note also that legal assessments will increasingly integrate sustainability concerns in the definition of what counts as ‘illicit’ when embedding the IFF agenda in the sustainable development framework. Altogether, these qualifications invite a shift in emphasis from legal categorisation to complex balancing tests, and from legal formality to anti-formalist, substantive legal approaches.
- 49 Qualified in this way, the definition of IFFs can accommodate different and competing definitional approaches and work streams in the IFF arena. Definitional details should not attract too much attention when discussing a broad IFF policy agenda. Note that other major reform packages, such as the BEPS programme, lack a clear definition of relevant concepts. Countries did not need to agree on the definition of ‘value creation’ to endorse the BEPS standards. The definitional uncertainty surrounding the term did not prevent the adoption of specific practical actions. The same type of ‘constructive ambiguity’ should play a role in the IFF definitional debate. Nevertheless, the definition can still be specified and eventually narrowed for specific policy or analytical purposes, as discussed below.

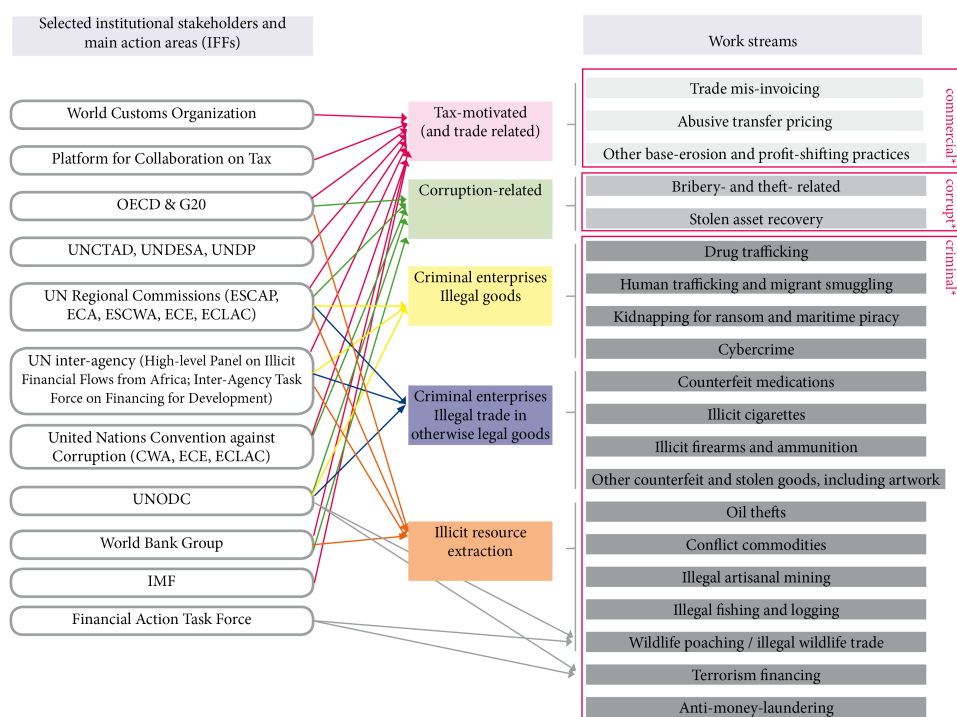
4.2.2 Adding Granularity to the Definition for Measurement, Research, and Policy Making Purposes

- 50 For specific policy and research purposes, it is necessary to add granularity to the definition, spelling out what is or is not within its scope in terms of actors, transfer mechanisms or origin. This ‘scoping’ process is largely discretionary: drawing a line between what is in scope and what is out of scope is necessarily a subjective exercise, framed by considerations of methodological convenience and political sensitivity. Eventually, different stakeholders may use different working definitions of IFFs, tailored to specific analytical or policy purposes, yet remaining under a shared umbrella definition. Working definitions are customised; they come with a policy agenda attached to them (Miyandazi and Ronceray, 2018). But that is hardly contentious, as long as stakeholders are conscious of, and explicit about, the methodological choices and policy objectives that frame the scoping of their definition.
- 51 Some degree of pragmatism must also play a role when breaking down IFFs into workable ‘thematic’ modules, or into a taxonomy suitable and distinctive enough for measurement, particularly with reference to SDG indicators. This involves subdividing the existing indicator for IFFs described in the SDGs (Indicator 16.4.1 ‘Total value of

inward and outward illicit financial flows, in current United States dollars’), which aggregates all IFFs into different sub-indicators.³⁶ As acknowledged by the UN constituency, ‘separate analysis of channels or components is more beneficial in designing policy responses to prevent illicit flows’ (UN General Assembly, 2017, 2).

52 Here, it is important not to start from scratch, but rather to build on existing operational work streams. In other words, the taxonomy/categorisation exercise should move backward from what exists, in terms of work streams and institutional frameworks in the UN system and in related fora (Figure 1). These work streams include, among others, the Stolen Asset Recovery Initiative, the Conference of the States Parties to the United Nations Convention against Corruption, UNODC-related thematic areas, and operational frameworks on countering money-laundering and the financing of terrorism. The starting point should be a stocktaking of existing IFF-related work streams that enjoy a high degree of legitimacy, conducive to an exhaustive inventory of IFF-related thematic areas, with a mapping of the responsible agencies (see Miyandazi and Ronceray, 2018). The IFF agenda may then build on these thematic areas, spurring strategic alignment and close collaboration between task teams across agencies with distinct client engagement (IMF, World Bank, OECD, and several UN and UN-affiliated agencies).

Figure : IFFs—Main action areas.



Note*: The mainstream public discourse identifies three broad types of IFFs: commercial, criminal, and corrupt. In practice, the three categories overlap and intertwine.

Source: Authors’ elaboration. For an in-depth review of initiatives targeting IFFs at the African and EU level, refer to Miyandazi and Ronceray (2018).

53 Likewise, when establishing or fine-tuning IFF indicators, it is important to consider existing data sources, and structure indicators in a way that informs and guides policy reform. Specifically, the analysis should consider regulatory developments in the area of tax transparency, and the establishment of multiple transparency and exchange-of-

information frameworks for tax purposes. These disclosure frameworks generate new data and enable more precise measurement of particular aspects of illicit flows. For example, automatic exchange procedures in tax matters³⁷ generate data on offshore tax evasion. As discussed by Cobham and Janský (2018), this data can be used to create a specific ‘undeclared offshore assets indicator’.³⁸ Furthermore, disclosure laws on payments to governments, disclosure of tax avoidance schemes and exchange of advance tax rulings, country-by-country reporting, and the development of beneficial ownership registries shed light on relatively opaque practices. The OECD country-by-country reporting data, in particular, may be used to construct an indicator of misaligned profits.³⁹ It is worth considering to what extent national authorities may build on these transparency frameworks and procedures to feed such indicators (Musselli and Bürgi Bonanomi, 2019). The analysis will need to consider built-in limits to this use: stringent standards on confidentiality, data safeguards, and proper use of the information that strike a suitable normative balance between transparency concerns and taxpayers’ rights.

5. Conclusions

- 54 A broad IFF agenda is a powerful engine for systemic change. It counters the tendency, inherent in legal specialism, towards fragmentation and duplication; fosters regulatory coordination across a range of interventions; and promotes policy interventions that have multiplier effects across the whole spectrum of IFFs.
- 55 The ‘umbrella’ definition of IFFs should be anchored in law, rather than ethics, so as to give precise and objective contours to what constitutes ‘illicit flows’. The definition of IFFs as *cross-border transfers of money or assets connected with some unlawful activity* can be retained as the ‘common denominator definition’. It provides an umbrella definition for separate work streams corresponding to individual IFF sub-components.
- 56 Under the ‘umbrella’ definition, ‘unlawful’ should be flexibly interpreted. It should expand to encompass legal standards that go beyond bright-line rules, allowing scope for principled decisions, balancing tests, and circumstantial assessment. Further, the legal assessment should not be confined to the domestic law in force in the assessed jurisdiction: it should comparatively refer to legal developments in other jurisdictions and extend to rules and principles of public international law. By benchmarking illegality against legal standards that have attracted wide international acceptance, the IFF debate would remain anchored in law. At the same time, it would integrate evolving elements and level the playing field across countries with different lawmaking and law-enforcement capacity. If ‘illegality’ is constructed in this way, flows associated with aggressive tax avoidance may be deemed illegal and fall within the scope of the IFF agenda.
- 57 A development or revenue-impact approach offers a useful policy orientation to the IFF debate. Embedded in the sustainable development agenda, it assists in drawing a line between licit and illicit financial flows while incorporating an ‘impact perspective’. It is compatible and can be reconciled with a legal definition of IFFs that fully acknowledges the role of standards and balancing in lawmaking and law implementation. The integration of sustainability concerns calls for a shift from taxonomic rules to circumstantial legal standards, from categorisation to balancing, and from formalism to non-formalist legal approaches.

- 58 For specific policy and research purposes, it is still necessary to add granularity to the legal definition of IFFs, by spelling out what is or is not within its scope in terms of actors, transfer mechanisms or origin. The process is necessarily discretionary, in particular for reasons of methodological convenience and political sensitivity. It is imperative to spell out methodological constraints that dictate definitional choices, alongside the policy implications that each working definition carries.
- 59 A pragmatic approach should inform the disaggregation of the IFF agenda into workable modules and corresponding indicators. The starting point should be a stocktaking of existing IFF-related international initiatives (and/or initiatives with a high degree of legitimacy) conducive to an exhaustive inventory of IFF-related thematic areas, with a mapping of the responsible agencies. The IFF agenda may build on these thematic areas, spurring strategic alignment and close collaboration between task teams across agencies with distinct client engagement. The SDG indicator on IFFs should be divided into sub-indicators. To the extent possible, this should be understood as an effort to refine the indicator, rather than revise it, in order to avoid time-consuming consensus-building procedures. When refining IFF indicators, it is important to conform to established concepts and standards from economics and accounting. It is also important to consider the potential of new disclosure frameworks (AEOI, CbCR, etc.). These frameworks generate new data that may enable precise measurement of particular aspects of illicit flows. There are, however, built-in limits to the use of such data, including stringent standards on confidentiality, data safeguarding, and proper use of information.

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NOTES

1. The narrow definition essentially covers transfers associated with 'corruption, illegal natural resource exploitation, smuggling and trafficking, money laundering, tax evasion and fraud in international trade' (World Bank, 2016, 2).
2. For example, certain tax optimisation schemes that make use of offshore structures to get around an inconvenient law may still be technically legal, depending on the reach of domestic anti-abuse rules. The law may not be violated, but the transaction is normatively unacceptable, hence 'illicit', under a normative definition of IFFs (UNCTAD, 2014, 172-73; Independent Expert on the Effects of Foreign Debt, 2016, 4; Chowla and Falcao, 2016).
3. It echoes long-standing distinctions in legal theory between positivist and natural law approaches, and between *lex lata* and *de lege ferenda* perspectives. In legal practice, it hints at some rift between law and justice.

4. As reviewed by Oats and Tuck (2019, 567–571), the meaning of ‘tax avoidance’ depends on the context in which the term is used. In its widest sense, it covers all arrangements aimed at reducing, eliminating or deferring taxes. In a narrow sense, as used in this paper, it only encompasses ‘aggressive’ tax avoidance practices that artificially circumvent the law for the purpose of reducing tax liability.

5. This can occur through different channels and techniques, including income shifting through interest payment (offshore loan structures, hybrid loan/entity structures, interest-free loans, etc.), royalty payments (IP and cost-contribution agreements, two-tiered IP structures, patent box structures), strategic transfer pricing and treaty shopping (European Commission, 2015, 2017). These schemes may have a legitimate commercial purpose (legitimate tax planning) or can be implemented primarily to deliver a tax advantage (aggressive tax planning), depending on the circumstances of the case.

6. A rich body of research and theory points to a substantial indeterminacy of legal outcomes, particularly with regard to the results reached by adjudicators in legal disputes. For a critical discussion, see, for example, Kress (1989; 1990; 1992), Tushnet (2005) and Wozzley (1979). See also *infra*, footnote .

7. As regards *statutory construction* and *purposive interpretation*, courts generally interpret law provisions purposively. They do not apply a strict letter of the law approach, but instead read provisions in terms of the purpose of the law as a whole. By interpreting legislation purposively, the courts can disallow transactions that merely follow the letter of the law but not its intention. There are, however, limits to this process. Typically, rules of legal interpretation oblige courts to stick to the wording of the legislation when assessing the objectives of the legislature. Further, the interpretation of tax statutes is not straightforward, and it may be difficult to discern a reasonably clear purpose. Beyond statutory constructs, common law jurisdictions have developed *judicial doctrines to counter tax avoidance* (judicial anti-abuse doctrines). This goes beyond the purposive interpretation of statutes. It entails judge-made rules and guiding principles that emerge from the case law. In the United States, for example, courts (and the revenue authority) turn to several doctrines to deal with tax avoidance schemes—for example, ‘substance over form’, ‘sham transactions’, ‘business purpose’, ‘economic substance’, and ‘step transaction’ doctrines. Even where a taxpayer carefully engineers his, her, or its scheme to comply with all technicalities of a particular tax statute, courts could resort to these doctrines to re-characterise the scheme or deny tax benefits. The underlying principle is that technical compliance with the law is not enough, if against the spirit of the law. Similar techniques are used in other jurisdictions to void transactions, re-categorise transactions, or collapse a series of connected transactions into a single one. Finally, some civil law systems have *general theories of abuse of law* that prevent abuse. For example, Swiss law entails general ‘anti-avoidance rules’ (Article 2 (2) *Code civil suisse*, RO 24 245) that also apply to tax law. In particular, under deeply rooted abuse of law principles, the law cannot be used for purposes contrary to that for which it was provided—i.e. no law can provide for its circumvention.

8. McBarnet and Whelan (1991) focus on the problem of ‘creative compliance’, defined as ‘using the law to escape legal control without actually violating legal rule’ (at 848). They argue that ‘creative compliance thrives on a narrow legalistic approach to rules and legal control, on a formalistic conception of law’ and critically assess how far anti-formalist strategies can be pursued through reliance on general principles and general catch-all provision. Their analysis highlights the obstacles to anti-formalism. Harmon et al. (2015) consider the distinction between the letter and spirit of the law in relation to contract violation, drawing the following distinction: ‘while the letter of the law represents the explicitly documented expectations, the spirit of the law represents the undocumented, and often tacitly held, expectations’ (at 498). Since ‘contracts are inevitably incomplete’, the expectations arising from a contract can be either documented or not, falling into the letter or spirit of the law (at 498). This gives rise to two types of contract

violations—letter violations and spirit violations. Minto (2016) specifically focuses on ‘the spirit behind the letter of the law regulating cooperative banks’ as lying with ‘cooperative banks’ corporate vision, strategy and tactics’ that strengthen cooperative banks’ resilience to systemic shock (at 17 and 20).

9. Withholding taxes and exit taxes, though not technically anti-avoidance rules, also play a key role as an anti-abuse device.

10. There are many variants in the language of GAARs. Some generally target arrangements that have the sole or main purpose of achieving a tax advantage (for example, the GAAR enshrined in the EU amended anti-tax avoidance directive). Others more narrowly target artificial and contrived avoidance schemes that cannot be regarded as a reasonable course of action in business (for example, under the UK GAAR). An equivalent tax treaty approach is the ‘principal purpose test’ (PPT).

11. In the field of direct taxation, Switzerland’s criminal tax law makes a distinction between breaches of procedural obligations (violations des obligations de procédure, LIFD Art. 181), tax evasion (*soustraction d’impôts*, LIFD Art. 175), and tax fraud (*usage de faux*, LIFD Art. 186). Tax fraud is a qualified form of tax evasion, which implies the use of forged or falsified documents or the pursuit of other deliberate acts to cheat the tax administration. It is a criminal offense punishable by a term of imprisonment of up to three years or a monetary penalty. Tax evasion is a minor offense (a contravention) punishable by a fine, which can reach as much as three times the sum in tax evaded. See *Loi fédérale sur l’impôt fédéral direct* (LIFD) (RO 1991 1184) and Xavier Oberson (2008; 2016).

12. In adjudication, ‘law is indeterminate to the extent that authoritative [sic] legal materials and methods permit multiple outcomes to lawsuits’ (Kress, 1989, 283). In other words, the same rule may yield different legal outcomes. As reviewed by Hasnas (1995), the indeterminacy argument was originally developed by the legal realists on two grounds—that the law is fraught with contradictory rules and that it is always possible for a judge to interpret the rules or the facts of a case differently. The purpose was to determine that the judge is not independent with regard to external influences and personal value judgments. The indeterminacy argument was further developed by critical legal scholars, based on the argument that law is radically indeterminate, incoherent, and contradictory (see in this direction Gordon, 1984, and Kennedy, 1976).

13. In the United Kingdom, the Committee of Public Accounts (House of Commons) held hearings in 2012 to investigate ‘why some multinational companies pay little corporation tax despite doing a large amount of business in the UK, and why some individuals can get away with using contrived schemes to avoid tax’ (House of Commons Committee of Public Accounts, 2013, 3). The assessment found that there was no clarity over where firms drew the line between legitimate tax planning and aggressive tax avoidance, selling schemes that the firms considered would only have a 50 per cent chance of being upheld in court if challenged (House of Commons Committee of Public Accounts, 2013, 5-7).

14. The ‘tax gap’ is defined as ‘the difference between tax that is collected and that which is “theoretically due”’—an estimated USD 40.7 billion (GBP 33 billion) for 2016/17 in the UK, or 5.7 per cent of total tax liabilities (Seely, 2018, 9).

15. Before the tax arrangement is tested in court.

16. A good deal of uncertainty and administrative discretion can attach itself to the question of whether a particular tax arrangement falls within the intended scope of GAAR. The UK GAAR strikes down tax arrangements that ‘cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions’ (Finance Act 2013, c. 29, Part 5, Art. 207 (2)); the EU GAAR counters schemes that ‘having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of the applicable tax law, are not genuine having regard to all relevant facts and circumstances’ (Article 6, Council Directive (EU) 2016/1164 of 12 July 2016, OJ L 193, 19.7.2016, p. 1). In order to mitigate

uncertainty of legal outcome, general anti-abuse rules are often associated with ‘pre-clearance mechanisms’, whereby the taxpayer can approach the tax authority in advance and obtain a ruling as to whether particular arrangements fall under the GAAR. Case law and reliance on advisory panels to delineate abusive arrangements also reduces uncertainty.

17. On rules and standards, see Sullivan (1992) and McBarnet and Whelan (1991). See also Section 3.2.1 *infra*.

18. It remains open to question whether these anti-abuse principles, recognised in a wide range of national legal systems, amount to ‘general principles of law recognised by civilised nations’ under Article 38 of the Statute of the International Court of Justice.

19. Rules ‘bind a decision-maker to respond in a determinate way to the presence of determined triggering facts’ while standards ‘collapse decision-making’ into principled decisions that apply a law’s purposes or principles to a fact situation (Sullivan, 1992, 58). In practice, there is a ‘continuum’ between rules and standards, as rules may to a varying extent integrate standard-like language (Sullivan, 1992, 61).

20. Refer to footnote above. To put it clearly, the ‘substance over form’ doctrine makes the incident of taxation dependent on the economic ‘substance’ rather than the legal form of a transaction. A typical example involves the debt vs. equity distinction: if an investor mischaracterises an equity contribution (non-tax-deductible) as debt (in which case the corporation may deduct interests payable on the debt), the court may re-characterise the debt as equity for tax purposes, disallowing the interest deduction.

21. Note that the revenue impact of these practices is not straightforward. For example, tax incentives may erode a country’s tax base, but also attract additional investment: the net revenue impacts should be assessed on a case-by-case basis (Matteotti, 2018).

22. A broad IFF agenda is advanced by the African Union, the Economic Commission for Africa, African Development Bank, Thabo Mbeki Foundation, African Capacity Building Forum, African Tax Administration Forum, Tax Justice Network-Africa, Pan African Lawyers Union and other civil society organisations.

23. United Nations Sustainable Development Summit, New York, 25–27 September 2015, *Transforming Our World: The 2030 Agenda for Sustainable Development*, UN GA Res. 70/1 (adopted on 25 September 2015), downloadable at http://www.un.org/ga/search/view_doc.asp?symbol=A/RES/70/1.

24. Third International Conference on Financing for Development, Monterrey, N.L., Mexico, 8–22 March 2002, *Addis Ababa Action Agenda*, UN GA Res. 69/313 (adopted on 27 July 2015), downloadable at http://www.un.org/ga/search/view_doc.asp?symbol=A/RES/69/313&Lang=E.

25. Soft law goals and objectives assist in interpreting and applying international law rules, and shape the emergence of new rules under international law and domestic law. They are formally relevant in interpreting treaty law as ‘context’, under Article 31 (3) of the Vienna Convention on the Law of Treaties (VCLT), if they find expression in a discernible pattern of acts and pronouncements. They can also be relevant as a supplementary means of interpretation, under Article 32 of the VCLT, when a consistent pattern is not discernible. At the domestic level, they may frame and prompt law reforms aimed at enabling effective implementation of the SDGs.

26. Such ‘particularisation’ of the law is rooted in equitable constructs. On the role of equity ‘as a basis for “individualised” justice tempering the rigours of strict law’, see Schachter (1982, 74). See also Schwarzenberger (1966), Cottier (2015), and, for an application to international trade law, Musselli (2017).

27. This results from the fact that ‘sustainable development policies are generally located “somewhere in between”’, and prompt questions as to the substantive coherence of legal regimes (Bürgi Bonanomi, 2015b, 30).

28. Article 6(1) of the International Covenant on Civil and Political Rights states that ‘[e]very human being has the inherent right to life’. The right to life is inextricably linked to the rights

guaranteed by the International Covenant on Economic, Social and Cultural Rights, such as the right to food, the right to shelter, or the right to water

29. When a state has ratified the relevant human rights instruments, its courts may uphold human rights as excuses for otherwise wrongful acts, to the extent that judges are required to enforce domestic laws in ways that do not encroach on a state's obligation to respect human rights.

30. In particular, countries whose tax policies have adverse livelihood impacts on other countries may stand in breach of their duty of international cooperation and assistance, as enshrined in the UN Charter (Articles 55 and 56), the Universal Declaration of Human Rights (Article 28), the Convention on the Rights of Persons with Disabilities (Article 3), the Convention on the Rights of the Child (and Articles 4, 24(4) and 28(3)) and the International Covenant on Economic, Social and Cultural Rights (Articles 2(1) and 11(1)) (Luisiani and Cosgrove, 2019).

31. Under the 'no harm' principle of international law, a state is duty-bound to protect other states from harmful effects caused by activities within its territory. The principle has been applied in relation to transboundary environmental harm and international watercourses.

32. Some developments move in this direction. Interestingly, the 2015 AAAA includes a commitment by member states 'to assess the impact of their policies on sustainable development' and Article 208(1) of the Lisbon Treaty obliges EU Members to take development objectives into account in the implementation of sectoral policies. A growing number of experts argue that countries have a duty under international law to assess and redress the potential extraterritorial impacts of their laws, policies and practices (ETO Consortium 2013, 7 (Principle 14)).

33. Teubner (1983, 256). On legal formalism and anti-formalist responses in accounting and taxation, see McBarnet and Whelan (1991).

34. In accounting and taxation laws, anti-formalist approaches entail 'capturing and controlling the substance rather than the form of a real life transaction or relationship, and implementing the spirit rather than the letter of the law' (McBarnet and Whelan, 1991, 854).

35. The last of these include, for example, exchange of information between tax authorities, whether automatic or on request; disclosure of tax avoidance schemes and exchange of advance tax rulings; country-by-country reporting; and the development of beneficial ownership registries.

36. Splitting the SDG indicator into different sub-indicators may amount to a refinement or a revision, depending on whether small or substantive changes are involved. While refinements of SDG indicators do not require formal adoption by the United Nations Statistical Commission (UNSC), revisions will be considered twice, in March 2020 and in March 2025, for formal adoption by the UNSC after global consultation. Different indicators should capture different types of IFFs, by component and channel. Some even argue for 'modularity' of IFF indicators, so as to factor in the context-specific revenue and development impacts of IFFs, and for 'politically actionable indicators', allowing for targeted anti-IFF strategies in specific local contexts (Khan and Andreoni, 2018).

37. This refers to the Standard for Automatic Exchange of Financial Account Information, developed by the OECD with G20 countries.

38. Defined as 'the excess of the value of citizens' assets declared by participating jurisdictions under the OECD Common Reporting Standard, over the value declared by citizens themselves for tax purposes to their tax authorities' (Cobham and Janský, 2018)

39. Calculated as 'the total excess profits declared in jurisdictions with a greater share of profits than would be aligned with their share of economic activity' (Cobham and Janský, 2018)

ABSTRACTS

This article reviews and challenges some key tenets of the debate on illicit financial flows (IFFs), and articulates some lines of legal reasoning that can help to define the boundaries of what constitutes illicit flows (or not). The analysis challenges the ‘narrow’ definition of IFFs, arguing that it mis-characterises the legal terrain. It then brings much-needed clarity to the ‘broad’ definition of IFFs, by anchoring it in legal concepts, rather than ethics. The analysis tackles two further contested areas in the debate: the tension between ‘development’ and ‘legal’ approaches to IFFs, and aggregate *versus* disaggregate approaches under the IFF agenda. In these areas, the analysis briefly rehearses the state of the debate, questions some entrenched assumptions, and presents ideas that help to reconcile conflicting views. It bridges development and legal perspectives by firmly embedding the legal discourse in the Sustainable Development Agenda and the SDGs. It concludes with some summary observations.

AUTHORS

IRENE MUSSELLI

Irene Musselli, Dr. iur., is a senior researcher and policy advisor at the Centre for Development and Environment of the University of Bern.

ELISABETH BÜRGI BONANOMI

Elisabeth Bürgi Bonanomi, Dr. iur., Attorney at Law, is a senior lecturer in Sustainability and Law and a senior researcher/policy advisor at the Centre for Development and Environment (CDE) and the law faculty of the University of Bern.