TYPOLOGIES REPORT ON
TAX CRIMES AND MONEY LAUNDERING
IN WEST AFRICA

May 2012
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Executive Summary

1. In West Africa, more than half of tax revenue is lost to the grey economy.\(^1\) This is underpinned by largely informal and unregulated economies, which seriously constrains the ability of West African governments to collect the maximum tax revenues possible. Tax bases in West African countries are thus narrow particularly because the majority of their populations in informal and subsistence agriculture. Additionally, not only do many registered domestic – and some international – businesses pay little or no taxes, but also tax collection in the region is highly inefficient and seriously undermined by public corruption. Given the enormous financial tax revenue losses generated by tax crimes, and the resultant negative effects on development in West Africa, this typologies project aims to investigate and shed some light on the techniques and methods used by criminals to commit different types of tax crimes and launder the money generated. Based on the cases collected and analysed, key indicators and red flags are generated to assist tax enforcement officials and reporting entities in detecting cases of money laundering related to tax crime. The study is also aims to assist policy makers in designing or reinforcing their policies and strategies to counter tax crimes and related money laundering.

2. Considering the need for a broader understanding of tax crimes and related money laundering in West Africa, GIABA commissioned a wider study on “Tax Crimes and Money Laundering: Human and Economic Development Perspective”, involving 10 of its Member States, namely, Benin, Burkina Faso, The Gambia, Ghana, Guinea Bissau, Mali, Nigeria, Senegal, Sierra Leone, and Togo. The findings of this study provide the required background for this typologies project.

3. A typologies workshop was held on 19-20 September 2011 in Saly, Senegal, and was attended by participants from 14 out of 15 GIABA’s Member States who presented their respective country case studies. Using an Expert Workshop Log (EWL) (see attached annex), the experts at the workshop analyzed each case study with specific attention to highlighting techniques used to launder money generated by tax crimes. Based on the outcome of the analysis, the case studies included in this report were selected.

4. Analyses of the case studies provided evidence that:

- Tax crimes are among the major sources of criminal proceeds in West Africa.
- The increasing wave of tax crimes and money laundering and existing vulnerabilities of West African countries are serious concern.
- The lack of strong political will is a major impediment to the implementation of comprehensive tax reforms and AML/anti-corruption regimes, and entrenched corruption by state officials negatively affects taxpayer’s willingness to pay.
- Some GIABA Member States lack the requisite legal and institutional frameworks against tax fraud and other forms of tax crime.
- Criminals and criminal networks in West Africa use both basic and sophisticated techniques in carrying out tax fraud schemes and laundering the proceeds they receive.
- The predominance of the informal sector in the region has kept many taxable businesses and entities off the tax net with adverse consequences on tax revenue. The cash-based nature of West African economies facilitates tax evasion and related crimes.
- Tax regulation and enforcement frameworks in most West African countries remain deficient and need further reforms.

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\(^1\) Threat Assessment of Money Laundering and Terrorist Financing in West Africa, GIABA, 2010
• Inter-agency cooperation and coordination on money laundering investigation related to tax crime issues, particularly among tax authorities and Financial Intelligence Units (FIUs) is very weak.
• Need to improve enforcement, investigative and prosecutorial capacities of member States’ tax and other law enforcement institutions in order to effectively counter tax crimes and money laundering.
• The manipulation of import and export transactions and the use of professionals to manipulate financial statements to reduce tax liabilities are common techniques of tax fraud and money laundering.
• Investigation and prosecution of tax fraud and tax evasion cases in Member States countries do not consider the money laundering element of such crimes.
• Data on prosecution and conviction of tax fraud are scanty Member States.
• Porosity of borders in West Africa facilitates the laundering of the proceeds of tax and other related crimes.
• Government incentives with regard to tax exemptions are sometimes abused.

5. A number of recommendations were made to the different organs in order to address the challenges of tax crimes in the region.
Chapter 1: Introduction

1. The structure of the West African economies presents serious challenge to tax collection. Tax bases in West African countries are thus narrow particularly because the majority of their populations in informal and subsistence agriculture. Moreover, administrative weaknesses and complicated tax procedures hamper effective tax collection. Also, not only do dishonest individuals, businesses, and organizations exploit loopholes in tax regulations to avoid taxation, but also tax authorities lack the requisite capacities to determine taxable personal incomes and corporate profits. Pervasive corruption and weak governance, as evidenced by poor management and misuse of tax revenues, negatively affects taxpayers' compliance with tax regulations.

2. Studies have revealed that more than a third of tax revenue per average is lost to the grey economy in developing countries. For instance, Schneider and Enste (1999), while considering 76 developing, transitional and OECD countries, estimated the size of their parallel economies to be 39%, 23% and 12%, respectively. This is even worse in the case of the West African region, whose parallel economy is averaged at about 60%.

3. The huge size of the informal economy in West Africa requires attention to enable GIABA Member States design and implement appropriate policies and establish mechanisms that would effectively address the challenges posed by tax crimes and related money laundering. Similarly, the outcome of such studies will help GIABA to develop and implement need-driven capacity building programmes for its member States as part of technical assistance.

Scope

4. The scope of the typologies project considered tax crime as a major money laundering predicate offence that ranges from fraud by public official, to evasion and illegal avoidance by the taxpayer. The primary focus of this project is to reveal the methods and techniques employed by criminals to commit tax crimes and launder the proceeds generated. It is also designed to shed some light on the vulnerabilities that may facilitate the occurrence of tax crimes especially in state institutions.

Objectives

5. The objectives of this typologies are to:

   • Understand the methods and techniques used to commit tax fraud and launder the proceed generated and the main sectors involved;

   • Highlight the different typologies of tax crimes;

   • Identify from case studies, the potential ML related tax crime occurring and in which form;

   • Deepen the knowledge and understanding of investigative and prosecution agencies of how illegal proceeds generated through tax crimes are being laundered;

   • Identify relevant indicators and red flags to assist financial institutions and other reporting entities in making decision with regard to monitoring and reporting suspicious transaction on money laundering related to tax crime;
• Assist policy makers, as well as the legislative and judicial authorities to address vulnerabilities in tax administration.

Methodology
6. The study was led by the GIABA typologies working group. A typologies workshop was conducted on 19-20 September 2011 at Saly, Senegal. Members of the GIABA Working Group on Typologies (WGTYP) and experts from 14 out of 15 GIABA member States attended the workshop and presented case studies. Under the leadership of the GIABA WGTYP, each case study was evaluated by experts using an Expert Workshop Log (EWL). The EWLs were analyzed and based on the outcome of the analysis the case studies reported below were selected. Each case was analyzed and the money laundering features/techniques were highlighted.

Structure of the report
7. In addition to this introductory chapter, Chapter Two gives the background of the problem and reviewed available information from literature. The various case studies are reported in Chapter Three, whilst the key findings from the study are set out in Chapter Four. Chapter five concludes the report and sets out recommendations.
Chapter 2: Literature Review

Overview

8. A tax is a payment levied upon individuals and legal entities to support government and legislative authorities in providing public services in their various jurisdictions. The process of collecting such payment is known as taxation, and plays a critical role in the economic welfare of a country by way of helping its government to stimulate growth and development, promote equitable distribution of wealth, and among others. Taxation also serves as a major instrument for generating revenue required for meeting government’s domestic and international obligations.

9. In most developing countries where significant resources are needed to address development challenges, tax revenues are important sources of such resources. Indeed, the recent global economic and financial crises, which reduced the quantum of donor funds to developing countries and remittances by their citizens in Diaspora, shows the importance of rethinking revenue collection strategies with the aim of increasing tax revenues.

10. However, efforts by developing countries to establish effective and efficient tax systems are seriously constrained by their largely informal and commodities-dominated economies, weak political structures and administrations, systematic corruption in their state institutions, deficient legal and institutional frameworks for taxation, and lack of reliable data on employment, incomes and profits.

11. Money laundering is the process through which proceeds of tax crimes are hidden or transformed into legitimate assets. This, therefore, makes the study of the phenomenon of tax crimes a significant element for understanding some of the prevailing trends in money laundering.

12. Despite numerous tax reforms and the implementation of anti-money laundering regimes, tax crimes and money laundering remain major issues of concern. The two phenomena are underpinned by the lack of transparency and accountability in the use of public funds, high levels of corruption, low probability of detection due to weaknesses inherent in law enforcement and tax administrations, and insufficient domestic and international cooperation.

Excerpt from the findings of the report on Tax Fraud and Money Laundering in West Africa: a Human and Economic Development Perspective

13. Although taxation is the primary tool used by governments to raise funds for the most needed social and economic development in West Africa, it remains murky, particularly as transparency and accountability are low.

14. A risk assessment of money laundering and terrorist financing in West Africa conducted by GIABA in 2010, revealed that criminals realise an estimated USD43 million annually from tax evasion and tax crimes. Another GIABA study in the same year on the nexus between corruption and money laundering revealed that corruption is the second most important source of illicit money in West Africa.

15. Importantly, not only do tax revenues provide governments of developing countries with the much-needed funds for development, it also reduces their dependence on external
development assistance and helps create the requisite fiscal space through which they can promote economic growth. More importantly, the collection of tax revenue is central to the emergence of more effective and accountable states as it stimulates the process of negotiation and bargaining between states and society (OECD 2010:1, Levi (1988), Braugtigam et al (2008), Toye (2000), Tanzi (2006), and Fakile (2010)).

16. An exhaustive body of literature has established a general pattern of weak taxation effort in developing countries, as compared with developed countries. According to the World Bank and OECD, the average tax revenue to GDP ratio in the developed world was approximately 35%, compared with approximately 15% in the developing countries, and 12% in the poorest among them (OECD 2005 & World Development Indicators Database). Estimates by the African Economic Outlook show that the average tax revenue to GDP ratio in West Africa has stagnated around 17% over the last decade, with no sign of changing in the future. Underlying such low ratio are a number of factors, tax fraud has become the most notable.2

17. Tax fraud can take place both at the domestic and international levels. The domestic dimension takes the form of tax evasion, which occurs due to a large domestic shadow economy, while the international dimension involves profit shifting by corporations and offshore holdings of financial assets by private individuals (Fuest and Riedel 2009: 1). Importantly, international dimension of tax fraud is not be confused with illicit capital flight. Although the lack of comprehensive economic data in developing countries makes obtaining reliable estimates on the volume of financial losses to tax fraud difficult, tax fraudsters receive estimated USD385 billion annually. Specifically, an estimated USD 285 billion is generated from domestic evasion annually, with USD 50 billion from international profit shifting by corporations and USD 50 billion from offshore holdings of financial assets (Cobham 2005).

18. The analysis of responses to the 2008 and 2009 FATF Strategic Surveillance Surveys indicates that many FATF delegations, especially those from Europe, considered tax and excise evasion as one of the three major sources of criminal proceeds. To be sure, a number of typology studies conducted by FAFT-styled regional groups in Eastern Europe and the Asia-Pacific that preceded the Strategic Surveillance Initiative provided evidence of the immense illicit money generated by tax and excise evasion (FATF typologies reports 1995-1996, 1996-1997 and 1998-1999).

19. While there are deep concerns that the above scenarios of tax fraud and money laundering are beginning to play out in West Africa with potentially grave implications for economic and human development as well as regional integration, analysis and policy responses must be situated in the context of solid empirical evidence so as to be relevant and effective. Real cases of tax fraud and money laundering must be thoroughly and properly analyzed in order to reveal their extent, trends, and as well as the techniques used by criminals. Of particular importance is the need to adequately understand the relationship between tax fraud and money laundering in West Africa and the region’s economic and human development performance.

20. On the basis of the findings and conclusions of the tax crimes regional study, that report provided the following recommendations:

- Local authorities and other Stakeholders should raise awareness through collaboration with civil society groups in West Africa on taxation.

2 Visit http://www.africaneconomicoutlook.org/en/countries/ for the country reports
The legal frameworks of tax administration in the region should be updated so as to close up the loopholes that encourage tax fraud.

GIABA should support the training and building of the capacities of national regulatory and supervisory agencies, including Financial Intelligence Units (FIUs) and anti-corruption agencies, to effectively detect tax fraud and money laundering.

The fight against tax evasion should start with encouraging positive attitudes in West Africa societies, particularly among business people, traders, and tax officials, towards compliance with tax laws.

National authorities should be more transparent and accountable in their use of tax revenues in order to win the confidence of their citizens.

There is need to develop a guide for tax agents to enhance their morale and professionalism.

The working conditions of tax agents, including their salaries and other benefits, should be improved so as to discourage them from pocketing much needed tax revenues.

National policymakers should develop a unified single tax system in their respective countries.

Tax administrations need to be modernized across the region to enhance transparency and accountability of tax administration.

National tax authorities should develop centralized tax payers databases in to ensure continuous monitoring and compliance with tax laws.

National legislative frameworks should be revised to ensure include tax crimes as in the list of predicate offences for money laundering.

Tax administrators and law enforcement officials should be encouraged to collaborate and coordinate in investigating the money laundering aspect of tax crimes.

Policymakers and stakeholders should consider the formation of a regional alliance of tax administrators as a way of enhancing tax administration in the West Africa.

21. This typologies study was conducted in 2011, involving 10 Member States, namely: Benin, Burkina Faso, The Gambia, Ghana, Guinea Bissau, Mali, Nigeria, Senegal, Sierra Leone, and Togo. Among the findings are:

22. The tax laws and systems of West African countries are rooted in the colonial legacies bequeathed to them by their colonial masters. Despite having been reviewed and modernized to reflect contemporary realities, these laws and systems still contain loopholes that enable individuals, businesses, and organizations to commit tax fraud.

23. The pervasive lack of institutional and administrative capacities to enforce existing tax legislations in West African countries makes the fight against tax fraud extremely difficult. This is evidenced by extremely low rates of investigation, prosecution and conviction in the numerous tax fraud cases in the region.

24. The structure of West African economies, characterized by the existence of large informal sectors and dominance of cash-based transactions, makes them highly vulnerable to tax fraud and money laundering. Likewise, poor governance, underpinned by political corruption and institutional fragility, widespread tax illiteracy, porosity of borders and weak border
controls, provides a fertile ground for tax fraud and related crimes. This study reveal common aspects of the problem of tax fraud in the different countries, ranging from lack of compliance by taxpayers with tax laws to impunity of tax offenders, to the bad economic policies of the States (particularly in the area of investment incentives).

25. The most prevalent techniques and methods employed in tax fraud include document counterfeiting, tax evasion, diversion of tax collected by tax officials, over-invoicing, and manipulation of account books.
Chapter 3: Typologies and Case Studies

26. This chapter presents a number of case studies that illustrate the various methods and techniques used by criminals to commit tax crimes and launder the resultant proceeds.

Typology 1: Tax crime and ML through third party agents and legislative gaps

Case 1: Tax Evasion through Misuse of Tax Exemption

In 2009, Messrs AB and BK incorporated Company A in Nigeria and obtained the requisite business permits from the Corporate Affairs Commission) mainly to provide air management services in the country. Mr RI was hired as the company's President and Chief Executive Officer. To commence operation in the aviation sector, company A needed to register with the appropriate government regulatory institution X. However, because of the stringent conditions involved in obtaining Air Operators Certificate (AOC), Company A registered with Institution X as a private flight management company. Furthermore, to operate air flights, company A sought and obtained approval of company C to operate under its license under the private category.

NOTE (1)
Company C is dully registered with institution X and has Air Operators Certificate (AOC) to operate both the private and commercial categories. Nigerian aviation law permits air flight management companies to operate under any company dully registered by institution X with AOC. Air flight management companies operating under the private category do not charge taxes and are exempted from paying certain statutory charges to X.

NOTE (2)
Because A was registered by X as air flight management company, it was not recognized by X as operating flights. Under the arrangement between companies A and C, A was only recognized by C as operating under the private category and was not supposed to be providing commercial services. However, A was secretly providing commercial services to several clients, including an oil company, a state Government, two construction companies and other clients. Company A was charging these clients 5% VAT, 5%WHT and 5% Charter Service Charge. An investigative authority E, obtained information on the criminal activities of company A and commenced investigation. During investigation, the authority E contacted X to ascertain the true status of A, the clients to verify the nature of services provided and banks to see the financial flows in and out of A’s accounts. Investigation by E at X & C revealed that Company A was registered by X as a private flight management company. This implies that Company A:

- Does not have Air Operators Certificate (AOC);
- Can only provide logistics and support services;
- Can only operate under the private category arrangement based on its arrangements with Company C.

Under the arrangement with company C, company A should not:

- Have customers (being a private operator) and thus, cannot charge VAT and WHT;
- Pay Charter Service Charge (CSC) to X.
Confirmation from A’s clients revealed that company A provided them commercial services. Invoices issued by A to the clients further corroborated this fact. Scrutiny of invoices and records of A revealed that Company A charged all its customers VAT, WHT and Charter Service Charge. Claim that these charges were collected on behalf of third parties (other airlines) was denied by the third parties. All the third parties denied having any relationship with A. Further investigation by E revealed that company A had collected and converted to its use about N110 Million of VAT, WHT and Charter Service Charge (also a form of tax payable to X).

Source: Nigeria

Comments: Weaknesses in legal regime can create room for criminals to exploit the system. In this case, the laws provided alternatives for companies that do not meet the requirements for AOC to liaise with the qualified ones, to use their license as well as allow new companies up to 18 months from date of commencement of operations to pay its first tax. The period of moratorium was when the fraud and laundering took place. By ploughing back part of the illicit money into the business as well as sharing the remainder to the shareholders, the company was able to launder the tax evasion proceeds.

Case Illustration

Case 2: Appropriation of tax fraud proceeds using subsidiary company
Z is a hospitality business, providing a range of services including accommodation, conference spaces, office spaces, consumables and car rentals. It incorporated a subsidiary K which is a building cooperative society, primarily into property development and management. Z charges and collects VAT, WHT and service charge on all services provided and contracts awarded. An investigative authority M received information about the illegal activities of Z and commissioned an investigation into Z’s activities in 2009. M’s investigation spanned from 2006 to 2008.

Investigation by M revealed that:

- Z had made some tax payments to the tax authorities;
- Deeper scrutiny of Z’s records showed that Z paid less than its tax liabilities and also did not remit significant portion of taxes charged and collected from clients to the tax authorities;
- Most supplies to Z are made by close associates of management and the appropriate taxes are not always taken.

Interrogation of the external auditor and the chief accountant to Z pointed to management complicity. The evasive and uncooperative attitude of the management to make records available and also make clarifications during the investigation led to the arrest of the Managing Director, F who confessed of maintaining multiple accounting books and confirmed presenting the wrong information to the auditors leading to the under payment of taxes.

Further investigation by M revealed that significant part of money made by Z from its business are paid into the account of its subsidiary K, to understate the income of Z and deceive authorities into believing that Z does not make sufficient profit just to pay less taxes. It is important to note that, because Nigeria is a cash based economy, Z accepts cash payment from its clients and such payments are made directly to the account of K. M’s investigations established that Z charged and collected taxes worth N6.5 Million and fraudulently laundered same to its subsidiary account through direct cash lodgements.

Source: Nigeria.

Comments: This case highlights the vulnerability of cash and subsidiary companies to money laundering. It also brings to fore the issues of weak tax inspection and the practice of maintaining multiple accounting books by criminals to evade tax.
Case 3: Tax Fraud/Evasion through manipulation of financial records and collusion of related Companies

The Customs Director General commissioned an audit of Company *JF, Ltd.*, in compliance with Customs obligations for the year 2008. An “off-shore” private company that started its activities in Cape Verde in 1995, dedicated to imports, sales and distribution of various consumption goods in close door regime. Its main provider is “CVI, Ltd.” which is the major shareholder of “*JF, Ltd.*”, with 90% of its capital. Various documents regarding fixed term deposits, service providers and purchases were analyzed, in order to verify the amounts transferred to the service providers, the orders placed by credit, and the amount of purchases made during the fiscal year 2008, with the following results:

- With regard to purchases, the total invoices presented to the Customs was 124,994,861.00 escudos but the declared amount in the company’s accounts was 124,987,213.00 escudos, resulting in a difference of 7,648.00 escudos, deducted in the company’s accounts upon receipt of a credit note, after the declaration of the merchandise.

- Concerning the cleared freight, the amount was 18,880,765.00 escudos, different from the amount found in the accounts of the company, which was 20,020,085.00 escudos.
• Other expenses were also found in the source documents, namely, BAF, freight overtax, THC, etc., counted as cost of merchandise totalling 4,219,541.00 escudos that was not declared in their respective customs import clearances.

• Costs of Marketing and Advertisement were also accounted for as cost of goods, which was, according to the company, billed to them by another company named “PBX Ltd.” According to purchases made with “CVI, Ltd.” the total amount was 51,166,707.00 escudos, calculated based on the supporting documents, regarding each purchase, recorded in the company files and not declared at the customs clearances.

The findings of the audit team are summarised in the table below. A total of 56,483,919.00 escudos, representing taxes and customs duties was not declared.

<table>
<thead>
<tr>
<th>DESCRIPTION</th>
<th>DECLARED FIGURES</th>
<th>FIGURES REGISTERED AT THE ACCOUNTS</th>
<th>DIFERENCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Invoices FCV “CVI, Ltd.”</td>
<td>124,994,861,00</td>
<td>124,987,212,88</td>
<td>7,648,12</td>
</tr>
<tr>
<td>Freight Expenses</td>
<td>18,914,765,00</td>
<td>20,020,084,76</td>
<td>-1,105,319,76</td>
</tr>
<tr>
<td>Regular Expenses</td>
<td>0</td>
<td>4,219,540,75</td>
<td>-4,219,540,75</td>
</tr>
<tr>
<td>Invoices “PBX Ltd.”</td>
<td>0</td>
<td>51,166,707,00</td>
<td>-51,166,707,00</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>143,909,626,00</strong></td>
<td><strong>200,393,545,39</strong></td>
<td><strong>-56,483,919,39</strong></td>
</tr>
</tbody>
</table>

The documents examined also showed that since its establishment in Cape Verde, in 1995, the company has been consciously omitting the values related to marketing and advertisement; billing them separately and afterwards considering them as cost of sold goods after customs clearance, supported by a contract of supposedly dubious legal value, established between “JF, Ltd.” and “CVI, Ltd.”, apparently pertaining to the same group, concealing the real transaction figures.

Source: Cape Verde

Comments: In this case, company JF Ltd was colluding with its principal owners, CVI Ltd to misrepresent financial records to the authorities in Cape Verde. These acts are deliberate and aimed at reducing its tax liabilities. By not making correct declarations and presenting fictitious records, JF Ltd was able to evade tax.

Case 4: Tax Fraud through Transfer Pricing

A national production company owned by a foreign group for the purpose of sourcing raw materials. To ensure normal production, the domestic subsidiary places regular orders for raw materials to their branch abroad which charges a price well above market prices. Once the bill is paid by the domestic subsidiary, it increases the costs of the national company, thereby understating its taxable profit, resulting in a tax evasion related to transfer pricing between a domestic company and its parent company holding 100% of its assets.

It is important to note that:

At the Group level: The transferred funds are received as interest on sales of raw materials. Such interest is either placed in banks as savings or transferred to the domestic subsidiary as a
At the domestic subsidiary level: The funds are transferred as a loan against payment of interest while the subsidiary does not need subsidy, given its yearly profits. Thus, once provided by the group, the funds are either re-invested in gainful activities other than its core business, such as starting up insurance companies or placing it in savings or partner accounts.

Source: Guinea

Comments: The unethical practice of transfer pricing / over-invoicing for the purchase of raw materials by the foreign group upon an order from the domestic subsidiary causes a large transfer of funds to the foreign group thus reducing the taxable income of the domestic company. This enables the domestic company to evade tax. This has been the common trend, especially amongst the multinational companies, within the region.

Typology 2: Tax crime and ML through partial exemption due to direct dealings with government

Case 5: Tax Fraud through Abuse of Government Incentives

X is a company involved in Construction and Civil Engineering activities in Nigeria. Company X’s major clients are the Federal and state governments. Company X sought and was granted some concessions for tax and import duties on importation of heavy construction equipment to enable it meet project dead-lines. The projects were awarded by the Federal Government. While the concession applies only to importation of heavy construction equipment, X applied the concession to all areas of its operations and items imported. Concerned citizens petitioned appropriate authorities on the criminal activities of company X and the petition was forwarded to an investigative authority B. B also got intelligence that further facilitated its investigation.

During the investigation carried out in 2010, B scrutinized the records of X to ascertain its level of compliance with the requirements of the tax laws and establish any money laundering crime. Investigation by B revealed that Company X had been investigated by the tax authorities and found to have evaded tax. Assessment Report of the tax authorities indicated that Company X evaded tax to the tune of about N1.6 billion between 2003 and 2007. Further investigation of the books of Company X revealed that the management of company X deliberately abused the concession granted by the Federal Government by applying the concession to other areas not covered by the incentive just to reduce their tax liabilities. Auditing firm (T) that prepared the financial statements of X absolved themselves of any complicity, claiming they acted or prepared the financial statements based on information presented to it by the management of X, believing that X has tax exemptions. B’s findings showed that the abuse of the concession reduced the tax liability of X by N1.6 Billion. X’s willingness to pay the ‘tax fraud amount’ without B taking the matter to court, shows the intention to defraud the government.

Source: Nigeria.

Comments: Weak regulation creates opportunity for criminals to perpetrate tax fraud as well as launder the proceeds of the tax fraud.
Case 6: Tax Fraud through Abuse of Tax Exemption

This is the case of a construction company that won a public contract to build 150 units of social housing, 20 small dams and irrigation works in 2010. The company was exempted from paying VAT and the business licence and registration charges worth 3% of the contract amount. The quantity of cement and reinforcing rods to be imported or bought on the local market was calculated and the end of the exemption clearly stated. However, after examination of the company’s records by the country’s intelligence service, it was discovered that the company exceeded the authorised quantity of imports by more than half. The evaded duties were levied with penalties.

Source: Mali

Comments: A close monitoring of government incentives could avoid tax fraud/evasion. This underscores the importance of effective supervision / regulation by tax administration.

Typology 3: Tax crime and ML through trade

Case 7: Understatement of Import Value to Reduce Tax Liabilities

In 2009, the CENTIF issued a report to the State Prosecutor of the Dakar Regional Court. The STR involved an amount of 1,186,494,95 FCFA francs transferred by a Senegalese businesswoman (OT). This referral followed a customs investigation of goods imported by OT, which were well over the amounts transferred in payment of the received goods. Note that a businessman can order goods and make payment through bank transfer after getting prior statement of imports with the inspection company COTECNA.

COTECNA deals with the implementation of the import audit programme. It has made prior import statements and import certificates on behalf of OT, which made it possible to use the banking system to transfer funds mainly to China. Yet, the customs investigation found that Chinese nationals made payments to the account of OT without any clear economic justification. The verification made showed that the amounts transferred were much higher than the value of goods actually imported. Before Custom officers and during the investigation, the lady admitted she had understated the value of the goods on the customs declarations to pay less tax.

Source – Senegal

Comments: This case illustrates the level of complexity that can be added to the detection and/or investigation of trade-based money laundering cases. It also highlighted the connection between trade-based money laundering and tax fraud/evasion and how import documents could be manipulated to facilitate the laundering of proceeds of crime.

Case 8: Tax Evasion and Money Laundering through Funds Transfer Agencies

In early 2011, Customs investigators arrested a Chinese national, WW who was dodging the conventional banking system to pay his foreign suppliers in breach of the provisions of Regulation 09/98/CM/UEMOA and Direction O2/99 RC that make it mandatory for such
transfers to be done through a bank. WW was rather using fund transfer agencies.

The amount of transactions made on behalf of his company was estimated at 1,021,832,000 cfa francs. This amount was beyond the control of money exchange. The monies actually came from compatriots of the accused from whom he would collect payments to be transferred back home under the guise of payments for prior import declarations. They were actually fictitious.

Through his company, WW was centralizing sums of money, getting import declarations and transferring money outside the conventional banking system. This practice was not only a means of moving money whose origin may be difficult to justify, but also facilitates tax evasion.

Source - Senegal

Comments: In this scenario, instead of simply wiring the funds to his suppliers, W.W chose to minimise the risk of detection through the use of the international financial system. This case illustrates the vulnerability of the informal sector, particularly the unregulated funds transfer agencies to money laundering and how this sector could be used to evade tax and facilitate money laundering. The transnational services offered by some of the operators in this sector create weaknesses that are exploited by criminals to facilitate trade-based money laundering and tax fraud/evasion.

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Case 9: Tax fraud through Manipulation of Books and Records

The Director General of the Tax Department ordered an audit of the ‘‘XPTO Corporation’’ whose main activities are Import and Advertisement Services, in line with the prevailing legislation on corporate tax compliance and the confirmation of the declarations made by XPTO corporation in 2008.

XPTO Corporation’s financial records were reviewed in relation to Single Tax on Income (STI) and Value Added Tax (VAT) Regulations, the National Accounting Plan and Domestic Laws on Tax. Information collected from the related services, namely, the Customs Department, Finance Department; Town Councils were taken into consideration as well as the bookkeeping records of the previous fiscal years. Investigations revealed that:

- The volume of import made by XPTO Corporation, Ltd. during 2008 totalled 27,973,835.00 escudos, while declaring only 1,265,365.00 escudos; as a result there was an under-declaration of imports totalling 26,708,470.00 escudos.

- The omitted imported products declared out of the accounting system, generating a discrepancy of 22,872,503.00 escudos, a margin of 86% of the corporation’s financial statement.

- A bunch of false invoices were identified in names of various entities that denied issuing such documents in lieu of purchases made on the domestic market. Thus, a net amount of non-existent purchase amounting to 41,961,282.00 escudos was discovered.

- Concealed purchases in the form of deducting the unpaid VAT, by introducing false invoices in the accounting system, an amount of 6,294,191.90 escudos to make controllers believe that VAT was paid.
There was an existence of VAT on non-declared sales of 378,956.00 escudo. Also, the following were observed:

- Cutting down of VAT - A mismatch was found between the amount of the VAT supported and the declared amount, totalling 1,455,338.00 escudos. This means that there were sales whose actual amount was not declared.
- Inflation of Cost - with regard to the communication, food and body hygiene accounts amounting 1,577,120.00 escudos; an amount which was later cut down to 473,135.00 escudos
- Declared Result by XPTO Corporation Ltd was 24,154,706.00 escudos.
- Tax default found out by the Tax Inspection Department was 89,461,626.00 escudos.
- Tax adjustment was 65,306,920.00 escudos.

Decisions:

The XPTO Corporation Ltd. was to reimburse to the treasury the sum of 8,128,485.80 escudos related to concealed purchases; reduction of VAT and VAT on non-declared sales or additional settlement; and pay the sum of 65,306,920.00 escudos, corresponding to the difference of STI.

Source: Cape Verde

Comments: Manipulation of companies’ books and records is one way unscrupulous entities adopt to reduce their tax liabilities and evade tax and launder funds.

Case 10: Tax Evasion through Under – Invoicing of Imported Goods

The Anti-Fraud Division of the Customs Department, conducted a detailed review and control in advance of declarations on imported commodities for consumption, to determine whether the customs taxes were paid by 'commercial firm PTS' that deals in import and export of staple food.

- The Customs Department, through its Anti-Fraud Division, requested supporting documents from its Portuguese counterpart, on products imported by firm PTS. Thanks to the existing Mutual Legal Assistance between the two Customs Administrations;
- An assessment was made on the declared values of the goods imported for consumption, the amounts paid, the real due amounts and the lowest possible amounts.
- A wide discrepancy was found between the declared values in imports as well as in the payment of taxes and other related customs duties;
- After auditing accounts of the company and establishing the right amount to be paid, it was concluded that Cape Verde Finance registered a loss of 26,129,644.00 escudos, due to under-billing of the imported consumption goods;
• Due to under-invoicing, firm PTS evaded payment of tax and other related customs duties totalling 32,674,556.00 escudos, by paying only 6,544,912.00 escudos.

Decision

The “Commercial Firm PTS” was subjected to a fine of 10,000,000.00 escudos. The Firm was also to pay the outstanding tax and all related duties in the sum of 26,129,644.00 escudos, through the correction of declarations of imports values.

Source: Cape Verde

Comments: This scenario highlights the connection between tax evasion/fraud and trade-based money laundering. The under-declaration of the value of the imports of the company was intended to reduce its tax liabilities and thereby evade tax.

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Case 11: Tax evasion through Trade-based and under declaration of transaction

El Nabil and his wife Zeinab Gentille, a couple from country A in the Middle East, set up a company known as HURAM which specialised in import/export of goods from country B in West Africa. They also became owners at the outset of a Chawarma restaurant, and posted a turnover of 10 million dollars after less than two years in business. The number of restaurants increased five-fold. Business was good. They set up 4 new branches in other West African states. However, to increase their profits further, El Nabil and his wife decided to find a way to avoid paying company tax. With assistance from an Asian company that supplied them goods, the couple developed the following complex system: company HURAM issues two invoices, the real one sent to El Nabil via DHL and the fake with a reduced amount sent to Zeinab Gentille, covering only a 10th of the value of the goods she presents to the Customs Service where she is known for her generosity from lower-ranked officers to highly-placed officials.

Since the couple followed the simplified and quick clearance procedure, they succeeded, in total, in avoiding paying the sum of 2 million dollars in customs duties and VAT. This organised tax fraud also helped the couple sell at a price lower than that of their honest competitors, since they, the couple, did not include the real costs corresponding to their prices. The additional profits generated by the tax fraud was used to finance the operations of the Chawarma restaurants, the cash income from which was paid into the company’s account and immediately moved to several personal accounts in order to lower the profits posted by the company at the end of the financial year.

While the couple were growing rich at the expense of the customs and tax authorities, their bank started having suspicions especially regarding the recurrent movement of large amounts to country A in the Middle East without any imported goods in return for the movements this time around. The documents presented to the bank by the couple were full with irregularities, especially regarding the excessively high values and quantities. The banking institution in question decided to file a suspicious report with its local FIU.

The analysis of transactions and review of financial flows led the bank to suspect the couple of tax fraud. With the help of the Customs Service, the FIU compared the amounts of the invoices
presented to the Customs Service with the amounts actually moved to the Asian company. The obvious difference between the two values clearly indicated that what they were seeing was a kind of tax fraud/evasion. Finally, the names of the couple appeared on the list of persons targeted by UN Resolutions.

**Source:** Cote d'Ivoire  
**Comments:** This demonstrates a case of collusion and manipulation of transaction records, particularly invoices to evade taxes. However, a key lesson is that cooperation amongst stakeholders – reporting institutions and regulators/law enforcement agencies is essential in combating the menace of tax fraud and money laundering.

Typology 4: Tax Crime and ML through mining exploration exemption and the use of PEPs/Professionals

**Case 12: Use of Professionals and Politically Exposed Persons (PEPs) to subvert processes, evade tax and launder funds**

A tax audit was conducted at a notary’s office leading to the discovery of a legal assistance and lobbying agreement between the Notary and the representative of a Cyprus-based foreign company. Obligations of the Notary include taking the necessary steps and getting the Presidential decree granting a mining exploration permit. The Notary was to be paid fees of 400 million CFA francs. The Notary obtained the exploration permit and withdrawals were made from the Notary’s bank account for the benefit of the regime’s high-ranking personalities. However, it was observed that the services performed by the Notary were not subjected to VAT, leading to conducting a Tax re-assessment on the Notary.

**Source:** Niger  
**Comments:** This case illustrates how gatekeepers and politically exposed persons can collude and subvert processes, facilitate or perpetrate tax evasion/fraud and money laundering.

**Case 13: Tax Fraud through “Serious” or “complex” Concealed work; small-scale gold panning and gold export counters**

Company X was granted gold exploration licences. Known officially as a player in the mining sector, it started hiring out exploration licences to companies Y, Z and F, which are all foreign companies. It gives priority to small-scale gold-panning operations. Its sizeable real estate and its gifts to various associations triggered investigations into the ridiculously low taxes being paid by X.

**Source:** Burkina Faso  
**Comments:** The priority accorded to small-scale-gold-mining operations (largely informal/unregulated - especially as no sale price is known on small-scale mining sites), deliberate investment in real estate (an unrelated business), close link and undue gifts to political and opinion
leaders, unusual relationship with automobile dealers (to launder proceeds from the sale of gold with the complicity of those who rent exploration licences) show the complexity involved in this tax fraud scheme.

The liquidation of the government body responsible for managing these aspects of mining despite a bright future that was always predicted for the mining sector in Burkina Faso further shows the involvement/complexity of the political class (politically exposed persons) in facilitating tax fraud/evasion by X. Generally, this case shows how companies can use complex web of schemes to perpetrate tax fraud and money laundering.

Case 14: Tax Fraud through a mining exploration company

As part of efforts to combat fraud and improve tax revenue, the tax authorities maintain a cooperative relationship with other government agencies, notably the customs authorities. It was following an exchange of import statistics that the Director General of Tax realised that a company that was on the list of major importers with more than 5 billion CFA francs worth of imports had never declared any business to the tax authorities. Investigations were launched and the records led to the identification of those involved in the matter. While nationals were formally identified, this was not the case with the alleged foreign investors.

Source: Burkina Faso

Comments: This case brings to fore the importance of inter-agency cooperation that is lacking in many jurisdictions, particularly amongst authorities involved in tax administration.

Typology 5: Tax crime and ML due to non supervision and monitoring

Case 15: Under-declaration of Income to Evade Tax

A company had been reporting earnings on the production of a particular agricultural produce over a period. A new company came into existence producing similar product with higher income reported to government. The product in question is very vital to the revenue sources of the Government. An inspection team was constituted to thoroughly examine the production process of the suspected company, including reviewing the inventory log, etc. The company was found to be under-declaring its income to reduce its tax liabilities.

Source: Liberia

Comments: In this case, the owners of the first company were under- declaring their income in an attempt to reduce their tax liabilities and evade tax.

Case 16: Tax fraud through exploitation of subsidies on essential goods

Koffi and Abou created in country A in West African coast a company known as Free Oil which specialised in the transportation of hydrocarbons. They started off with 2 used tankers of 60,000l
capacity each and were authorised by the oil refining corporation to transport petroleum products bought from the refinery free of tax at 200 cfa francs per litre and taken to countries B, C and D a thousand and 200 km away from the refinery. The sale price at the pump in country A is 600 cfa francs per litre including taxes.

In less than one year in business, Free Oil got out large quantities petroleum products declared to be exclusive of tax from the refining company for export to countries B, C and D. During an annual audit by the customs service on petroleum product export, it emerged that declared quantities of petroleum products transported by Free Oil stood at 43.2 million litres. However, investigations conducted in countries B and D revealed that no imports were declared on behalf of Free Oil. As for country D, there is only a foot bridge linking the two countries borders, meaning that all the exports declared by Free Oil were fictitious, leading to huge tax losses to the Government of country A estimated at billions of cfa francs. Consequently, there was a fraudulent dumping of petroleum products diverted from their designated destination and sold on the national territory without paying the applicable duties, taxes and royalties.

Source: Cote d’Ivoire

Comments: Shortcoming in the customs system of checking goods in transit created a loophole that the criminals took advantage of. This reinforces the observation that weak regulation of tax administration creates room for tax evasion/fraud.
Chapter 4: Key Findings, Indicators and Red Flags

Key Findings

27. The main findings of this typologies study are as follows:

- Tax crimes are major sources of criminal proceeds in West Africa.
- The increasing wave of tax crimes and money laundering and existing vulnerabilities of countries studied are of serious concern.
- Some GIABA Member States lack the requisite legal and institutional frameworks against tax fraud and other forms of tax crimes.
- Criminals and criminal networks in West Africa use both basic and sophisticated techniques in carrying tax fraud schemes and laundering the proceeds they receive. Among such techniques are maintenance of multiple accounts and financial records, transfer pricing, informal money transfers, under-declaration of incomes and profits, manipulation of import and export transactions, filing false tax returns including making false deductions, and among others.
- Proceeds from tax crimes in West Africa are laundered by way of investing them into legitimate businesses or mixing them with business profits, using subsidiary companies, using fictitious accounts to facilitate diversion of financial instruments and tax revenues, etc.
- The predominance of the informal sector in the region has kept many taxable businesses/entities off the tax net with adverse consequences on tax revenue. The cash-based nature of West African economies facilitates tax evasion and related crimes.
- Tax regulation and enforcement frameworks in most West Africa remain deficient and require further reforms.
- Inter-agency cooperation and coordination on money laundering investigation related to tax crime issues, particularly among tax authorities and Financial Intelligence Units (FIUs) is very weak.
- Insufficient political will and pervasive corruption were identified as major impediments to the implementation of comprehensive tax reforms, AML/anti-corruption regimes and taxpayer’s willingness to pay tax respectively.
- The pressing need for capacity building was identified for all authorities to improve enforcement, investigation and prosecution of tax crimes and money laundering matters.
- Tax fraud/evasion connections with other well-known money laundering typologies were identified such as trade-based money laundering and the use of professionals to manipulate financial statements to reduce tax liabilities/evade tax.
- In many countries, tax frauds/evasions are treated without integrating the money laundering element, particularly during prosecution.
- There is a paucity of data/statistics on tax crimes generally and related prosecution and conviction across the region.
- Porosity of borders in the region facilitates the laundering of the proceeds of tax crimes and other related crimes.
- Government incentives, particularly tax exemptions when not monitored are abused for tax fraud and related crimes.
Money laundering indicators and red flags

28. A number of indicators and red flags were identified based on the various case studies presented. These are outlined below:

a. Indicators:

- Non-remittance of tax proceeds by authorized tax collectors.
- Preference and usage of non-bank value transfer systems.
- Ostentatious and conspicuous lifestyles and sudden unexplained wealth.
- Maintenance of multiple financial and accounting records.
- Systematic reduction in tax revenue.
- Preference for cash transactions.
- Huge amounts involved in activities that have no link with declared activity, neither by income nor by the importance of the sector.
- Under statement of account by corporate entities.
- Structuring of employee salaries/entitlements to allocate substantial amount payable to non-taxable incomes/sub-heads.
- Former tax officials working as tax consultants for corporate high net worth companies.
- Consistent exceptionally good reports for corporate entities by tax administrators.
- So-called re-investment of large amount from profits before tax where zero tax provision on such investment exist.
- Unusual transactions without any economic justification.
- Revenue/income manipulations.
- Tax waivers for products or services that are monopolised by a few companies.
- Frequent interactions between company officials and particular tax officials (so called fixers).
- Importing goods into low tax country and then moving them to high tax country (profit based on tax rate).

b. Red flags:

- False declaration of merchandise and significant discrepancies between the values of the commodity reported on the invoice and the commodity’s fair market value.
- Award of bonuses that seem to exceed industry expectations.
- Use of acronyms to open bank accounts for diversion of official cheques.
- Transactions aimed at reducing tax liabilities, including transfer pricing.
- Use of two set of tax collection registration numbers
- Absence of value added tax registration number on receipts while the VAT has been claimed.
- Non-declaration on receipts of tax amount claimed.
- Use of different types of receipt to sell the same goods or offer the same service.
Chapter 5: conclusion and Recommendations

Conclusion

29. Tax administration in the West Africa region has undergone several reforms with countries operating multiple tax systems, ranging from VAT to customs duties. In spite of modest improvements in legal, regulatory and enforcement tax frameworks, as well as increase in tax revenue recorded in many countries, tax crime remain a major impediment to domestic resource mobilization with attendant adverse consequences on development.

30. This report is an attempt to understand the problem of tax crimes through case studies in order to develop appropriate measures to address the challenges for the purposes of optimizing tax potentials for development. The cases found are mostly on non-disclosure of true income and under invoicing in order to avoid paying tax or paying the right tax. While the threat for tax crimes exists, there are a number of vulnerabilities that facilitate the commission of these crimes such as weak institutional frameworks, misuse of public funds, unaccountable governance and corruption, among others.

Recommendations

31. As indicated earlier in this report, tax crimes and money laundering are major challenges that have deprived the West African region of resources needed for development. With the global financial crises and dwindling primary commodity prices, tax remains the most veritable and reliable source of revenue for governments. This typologies study was partly meant to identify the existing weaknesses on the preventive, regulatory and enforcement frameworks. It would lead to further reform of the tax administration systems or the strengthening of measures to minimize tax crimes and money laundering.

32. This study also shows the need for continued strong commitment, collaboration and cooperation amongst stakeholders involved in tax administration and management of AML regime in the region in order to fully optimize the potentials of taxation for development. The following recommendations are put forward for consideration:

State Authorities

33. Reforming and strengthening the Tax regulation is crucial and such reforms should be made public, sensitizing the taxpayers about the details. There is need to develop guidelines and interpretative notes on new regulations. It is also pertinent to criminalise tax evasion/fraud and include it as one of the predicate offences in the country’s AML/CFT laws. Heavy penalties should be prescribed for tax fraudsters. There is the need to increase cooperation and collaboration amongst tax administrators, law enforcement and other investigative agencies, and the judiciary, particularly in terms of information sharing and joint operations, as necessary, to improve enforcement, investigation and prosecution of tax related matters.

34. Greater political commitment to address the issue of corruption and improve transparency and accountability in the management of resources at all levels. Tax officials are in some cases not very transparent in disclosing tax rates or in their calculation of tax duties, thereby intimidating taxpayers and subsequently getting them into fraudulent activities at the expense of the State.

35. There is the need for state authorities to develop a national strategy to widen the tax base and possibly revise some rates downward taking into consideration rates charged in other jurisdictions (emulate best practices). Tax incentive should be given in the form of tax returns
charged on how much tax you pay and discourage tax exemption by given tax holiday and the like to prevent abuse.

36. One way of widening the tax base is by formalising the informal sector and incorporating it to be part of the tax bracket. The state should develop and implement measures to integrate the informal sector with the formal sector and work towards a cashless society that would check cash transactions above certain limits to enable audit trails and facilitate tax assessment.³

37. Tax is revenue to the State. By way of motivating tax payers, the authorities need to give feedbacks on what is collected and how it is being spent on infrastructural and social services to improve the lives of citizens and providing an enabling environment for the private sector to thrive. The latter has a multiplier effect as the growth rate of the overall revenue depends largely on it.

**Tax administrators, Investigative and Law Enforcement Agencies and the Judiciary**

38. Investigative agencies, in collaboration with the tax administrators should from time to time conduct net worth analysis on businesses/companies. The growth of businesses should match declared profit.

39. Automation of tax administration with a functional and user friendly website is required. The authorities need to provide a platform whereby tax client can freely access credible information and be able to calculate taxes due from them, even before tax official approach them for payment.

40. Tax education that could bring the taxpayer on the same level with officials is paramount. Tax authorities need to embark on public awareness and advocacy, targeting current and potential taxpayers on the essence of tax, types of taxes and their corresponding rates, as well as tax formulae and how they can be calculated.

41. Adherence to due diligence in recruitment processes, improved welfare and capacity development of tax officials is critical to curtailing corruption in tax administration and enforcement. Tax officials need to have the minimum basic qualification upon recruitment and appropriately train to specialise. They should be adequately paid and well motivated with other incentives.

**Regional Authorities**

42. At the regional level, ECOWAS should harmonise some tax rates so as to check cross borderer transaction that leads to tax evasion.

43. Tax administrators in the region should intensify their cooperation at the regional level to share best practices to enable them overcome challenges posed by fraudsters and evaders. This can be achieved through peer review of tax systems and by organising capacity building programs.

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³ See GIAB Typologies on Cash Transactions and Cash Couriers in West Africa, which can be accessed at: [http://www.giaba.org/reports/typologies/reports.html](http://www.giaba.org/reports/typologies/reports.html)
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Appendix: Case studies report form

INTER-GOVERNMENTAL ACTION GROUP AGAINST MONEY LAUNDERING IN WEST AFRICA

TYPOLGIES EXCERCICE ON:
Tax Fraud and Money Laundering in West Africa

REPORT ON CASE STUDIES

Name of Country ___________________________ Name of reporter ___________________________ Case No. ________________

A. Facts of the case (including what prompted the commencement of the investigation and status of the case as at the date of reporting):
### B. Money Laundering Features of the Case

Please, provide details on how any of the money laundering features outlined below has appeared in the case.

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<thead>
<tr>
<th>SN</th>
<th>Money Laundering Feature</th>
<th>Details of manifestation in the case</th>
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<tbody>
<tr>
<td>1</td>
<td>Formal banking system through financial products (including remittance/transfer, insurance, investment &amp; saving products etc)</td>
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<td>2</td>
<td>Non-banking formal value transfer systems</td>
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<td>3</td>
<td>Use of moveable goods</td>
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<td>4</td>
<td>Real estate (ownership and leasing of land and buildings)</td>
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<td>5</td>
<td>Cash couriers</td>
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<td>6</td>
<td>Informal value transfer systems</td>
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<td>7</td>
<td>Third party business structures, charities and other legal entities</td>
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<td>8</td>
<td>Retail payment systems and the ATM network, including new payment methods such as mobile, internet and card systems.</td>
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<td>9</td>
<td>Gatekeepers: Lawyers, accountants and other Professionals and insiders</td>
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<td>10</td>
<td>Involvement/use of Politically Exposed Persons (PEPs)</td>
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<td>11</td>
<td>Weaknesses in legal, regulatory, enforcement control/.geographical vulnerabilities</td>
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<td>Please, provide any additional information on any technique/method not mentioned above</td>
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GIABA Secretariat