Nexus between Illicit Financial Flows and Economic Development

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Abstract
The international movement of money illegally or illicitly generated in developing countries has become a major issue in the development agenda. Reducing illicit financial flows (IFFs) is now a component of Goal 16 of the 2015 Sustainable Development Goals, as well as a staple of declarations from the G7 and G20.Kenya has been losing an average of Sh40 billion every year through illicit financial flows since 2011 as both government, local firms and multinationals engage in fraudulent schemes to avoid tax payments. Combined, this is an increase from Sh160 billion recorded in five years to 2011, an indication that illicit trade is gaining momentum in the country at the time the state is struggling to meet its revenue targets revised to Sh1.64 trillion. The purpose of this research is to explore the nexus between gross domestic product and illicit financial flows in Kenya. Specifically, the paper sought to discuss illicit financial flows in greater detail to strengthen our appreciation of the phenomenon and clarify some key concepts associated with it including an understanding of the linkages between gross domestic product and illicit financial flows. The findings showed that the reform agenda forillicit financial flows IFFs has four major components: reporting of profits; listing of beneficial ownership of assets; automatic exchange of tax information and anti-money laundering (AML) provisions. Though supported by the Kenyan government and with a potentially effective enforcement mechanism (blocking non-complying countries from access to the international banking system), AML rules have been consistently poorly implemented. This reflects the poor alignment of incentives and institutions, both private and public where many major international banks have paid large fines for systematically flouting the rule. The IFF reform agenda needs to more carefully assess those governance problems in order to be effective. Countermeasures include institution building strategies, international cooperation and information exchange, and fiscal transparency. Development practitioners need to understand the nature of the problem of illicit financial flows as an obstacle to development, and be aware of interventions that can reduce such flows.

Key Words: Gross Domestic Product (GDP). Illicit Financial Flows (IFFs), Anti-money Laundering (AML).