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CONCEPT OF ILLICIT FINANCIAL FLOWS AND DOMESTIC RESOURCE MOBILIZATION

MARCH 2025

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EXECUTIVE SUMMARY

Following the promulgation of the 2010 Constitution, Kenya adopted a system of devolved government composed of 47 counties (subnational governments). Though the counties have fiscal powers to impose taxes and user fees, their tax mandate is limited to property and entertainment taxes. A significant portion of their revenue comes from the equitable sharing of national revenue raised by the national government. Therefore, illicit financial flows at the national government reduce funds that would otherwise be channeled to counties.

Revenue leakages of funds collected at the national government that would otherwise trickle down to county governments is attributed to many factors, corruption being at the core. At county levels, investigating the linkage between Illicit Financial Flows (IFFs) and corruption might be the key to unlocking the resourcing potential of devolved functions. Understanding the roles of shared institutions such as the Senate, Council of Governors, and the IBEC can play in combating IFFs is critical in fighting against this vice. To maximize domestic resource mobilization (DRM), a thorough examination of the anti-corruption laws and the legal framework for combating IFFs in general is necessary.

This report is premised on the need to provide information and a better understanding of existing laws and knowledge on IFFs and DRM. The aim is to underscore the need for shared institutions to support and push for the fight against IFFs and corruption. With opinions and views of key informant interviews to understand the effect of IFFs on DRM at the county level and policy views on the need for shared institutions to take part in curbing IFFs, the report endeavors to add value to existing works and provide insight on the Kenyan context.

Though Kenya has strived to seal loopholes for revenue leakages through initiatives such as Inter-Agency Anti-Illicit Trade Working Group, National Action Plan to Combat Illicit Trade 2019-2022, Joint Border Committees, National Baseline Survey on Counterfeit and other Forms of Illicit Trade in Kenya 2021, National Observatory on Illicit Trade Kenya, much needs to be done. Independent studies show that Kenya loses billions of revenue, for instance, a 2014 study funded by the Danish government indicated that Kenya's tax loss could be as high as 8.3 percent of government revenue, hampering economic growth and resulting in billions in lost tax revenue.

The two-level system of governance continues to face challenges in combating corruption and IFFs. However, a strengthened legal framework and an understanding of the roles of shared institutions in combating IFFs will go a long way in this fight. They were improving the efficiency of own source revenue (OSR) mobilization backed by clear and comprehensive laws on taxation at county level. Ensuring transparency and access to public information will increase accountability in public funds management as per domestic laws and international standards. A collective approach to combating IFFs, where all stakeholders from national level to the devolved systems, backed by evidence-based research, strengthened legal frameworks and continuous assessment of progress would be crucial to improve DRM.

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Images © Pixabay

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Global Financial Integrity

ACRONYMS AND TERMS

CBA - Commercial Bank of Africa

CRA - Commission on Revenue Allocation

DRM - Domestic Revenue Mobilization

EAC - East African Community

EACC - Ethics and Anti-Corruption Commission

EPZ - Export Processing Zones

FTZ - Free Trade Zones

GFI - Global Financial Integrity

GIS - Geographic Information System

IFFs - Illicit Financial Flows

IBEC - Intergovernmental Budget and Economic Council

OECD - Organization for Economic Cooperation and Development

OSR - Own Source Revenue

1 | INTRODUCTION AND COUNTRY CONTEXT

In 2010, 67% of Kenyans voted in favor of the adoption of a new constitution, which instituted a system of devolved government. The devolved governance system established a national and forty-seven (47) county governments (subnational governments) with a clear mandate of several functions as stipulated in the Fourth Schedule of Kenya's Constitution. To facilitate both recurrent and developmental expenditures, the county governments are expected to mobilize their own revenue through taxes such as property and entertainment taxes and as well as receiving funding from the national government through the equitable share established under Article 202 of the constitution of Kenya. The 2010 constitution also mandates the two levels of government to be assigned specific amounts of revenues to perform their respective functions. This exercise is undertaken every fiscal year through the Division of Revenue Act, based on the technical advice from the Commission on Revenue Allocation.

In mobilizing revenue, the counties are dependent on a number of factors, including, level of economic productivity in the county—mostly driven by the population size and demographics. For instance, the County Government of Nairobi, being the capital city and the center for business activities, tends to collect more revenues than other counties. Other considerations include the availability of natural resources. Counties' debts and financial obligations and local policies and regulations can also contribute to the counties' revenues. Ideally, counties are required to pull from their resources to fund their budgets and the projects they seek to undertake. However, more than half of the counties have continuously unsuccessfully met the set revenue target.

The trends in the collections since their formation indicate that very few counties have met the estimated revenue targets. In their inaugural financial year, 2013/2014, an aggregate of KES 26.3 billion in own source revenue was raised by the counties, translating to 48.5% of the total estimated revenues. The 2018/2019 financial year witnessed the highest percentage of 74.8% in collections against the set annual target of KES 53.86 billion. In 2021/2022, the counties collected a total of KES 35.91 billion in OSR, which was 59.4% of the annual target of KES 60.42 billion. Analysis of own-source revenue as a proportion of the annual revenue target indicated that four counties, namely, Lamu (10.5%), Vihiga (101.6%), Turkana (113.5%), and Migori (110.5%) achieved their set annual target while the rest did not as demonstrate in the chart below.

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[1] Kenya Law Reform Commission. Available at <https://shorturl.at/flmN2> Accessed on 10th October 2023

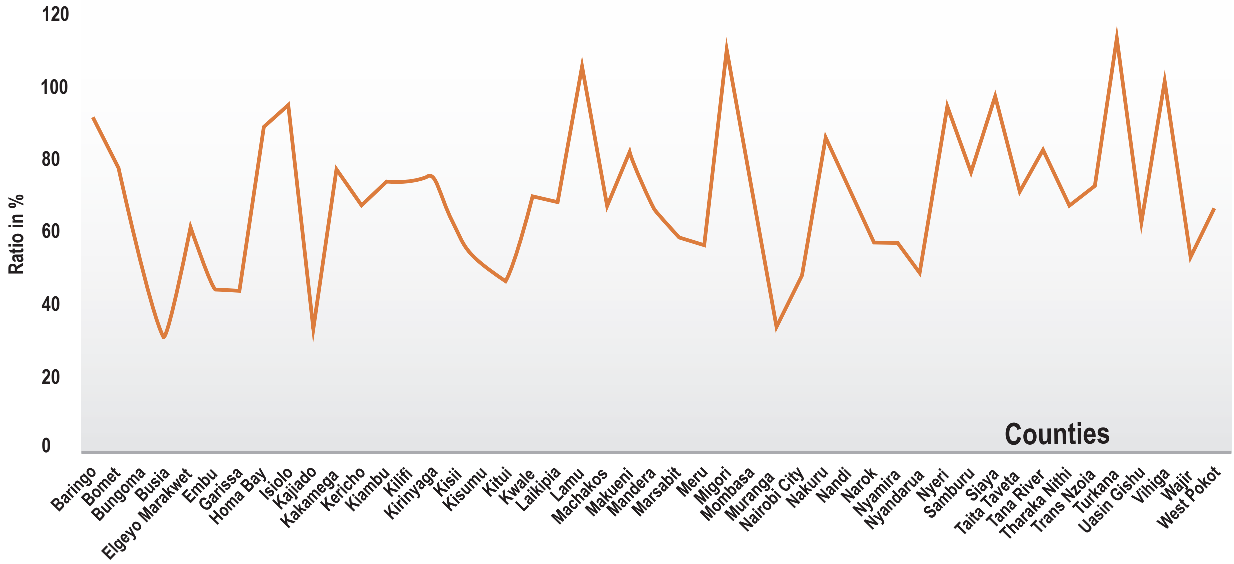
[2] 2023 Gross County Product (GCP). Available at < https://shorturl.at/iFLR9> Accessed on 10th October 2023.

[3] Revenue collection per county in Kenya - financial year 2021/2022, Afro Cave. Available at < https://shorturl.at/MNOR5 > Accessed on 10th October 2023.

[4] Revenue collection per county in Kenya - financial year 2013/2014, Afro Cave. Available at < https://shorturl.at/MNOR5 > Accessed on 1st October 2023.

[5] Revenue collection per county in Kenya - financial year 2021/2022, Afro Cave. Available at < https://shorturl.at/MNOR5 > Accessed on 10th October 2023.

Actual Revenue/ Annual Target (%) 1st July 2021 to 30th June 2022



Further, according to Article 202 of the Constitution, revenues raised nationally need to be shared equitably between national and county governments to ensure that both levels of government can perform their functions and that Kenyan citizens get the most out of public resources. On the equitable share to be allocated to counties, article 203(2) of the constitution sets a minimum threshold of 15% of all revenue collected by the national government. This indicates that any shortcoming during the mobilization of resources at the national government directly impacts the equitable share to be allocated to counties. Further, such shortcomings have a ripple effect on the general social and economic well-being of the population. Based on previous history, Kenya has been an interesting ground for evaluating the impact of political institutions on IFFs for a number of reasons. Firstly, evidence of reported grand corruption scandals involving IFFs by the ruling political elites from the late 1970s to the early 21st century.[7] Kenyans are concerned about corruption as a facilitator of IFFs that depletes public resources while raising the debt levels and undermining tax moral accountability between citizens and the State. This leaves a key question on whether the devolved system of government places the country in a vantage position to fight IFFs or otherwise. Additionally, a notable leakage and hindrance to the achievement of set revenue targets is IFFs that manifest through tax losses, corruption, illegal wildlife trade, and trade misinvoicing. For instance, between the years 2002 and 2011, Kenya experienced great development in her extractive industry.[8] However, within the same period, Kenya is believed to have lost as much as $1.51 billion to trade misinvoicing.[9] Additionally, a 2014 study funded by the Danish government noted

[6] County Governments Annual Budget Implementation Review Report. Available at < Counties-Sep-2022-web.pdf (cob.go.ke) > Accessed on 10th October 2023.
[7] Illicit Financial Flows and Political Institutions in Kenya. Available at < https://shorturl.at/aehQ2 > Accessed on 10th October 2023.
[8] Industries for Sustainable Development in Kenya. Available at < https://shorturl.at/ouHNO > Accessed on 10th October 2023.
[9] Report of the High Level Panel on Illicit Financial Flows from Africa. Available at <https://shorturl.at/lmtBU> Accessed on 10th October 2023.

Kenya's tax loss could be as high as 8.3% of government revenue, hampering economic growth and resulting in billions in lost tax revenue.[10]

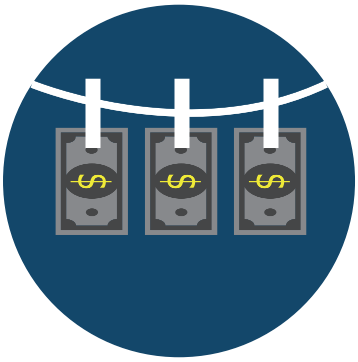
Regarding illegal wildlife trade, poaching remains one of the leading organized crimes that threaten security in the global arena, regionally as well as nationally.[11] The poaching crisis has been aggravated by weak governance, corruption and poverty. In Kenya, poaching is projected to increase and affect the country's economy and biodiversity if not addressed. The increase in poaching poses a challenge to economic development and the livelihoods of millions of people who depend on tourism for a living.[12] The national government plans to have county governments that host game parks receive 50% of revenue generated from game parks, which will be a major increase to the counties' OSR mobilization. Therefore, the starring role of IFFs and their adverse effect on the country's domestic resource mobilization cannot be ignored.

Even though no empirical evidence in Kenya has been presented to link the effect of IFFs on the county government's efforts in resource mobilization, the leakages experienced at the national level ultimately affect the equitable share transferred to the counties. Additionally, within the county corruption which is a key source of IFF is highly prevalent.[13] The most immediate impact of IFFs is a reduction in domestic expenditure and investment, both public and private. In real terms, this translates to fewer hospitals and schools, fewer public service providers, fewer roads and bridges[14] thus preventing the country from realizing the United Nations Sustainable Development Goals and national economic blueprints such as Vision 2030.

Therefore, this report scopes the existing laws that guide the fighting of IFFs, with a focus on how the devolved units can support the fight to yield more from their resource mobilization efforts. This report encompasses aspects of IFF on areas where policies and laws exist and where there is comparable data on compliance.

[10] Report of the High Level Panel on Illicit Financial Flows from Africa. Available at <https://shorturl.at/lmtBU> Accessed on 10th October 2023.
[11] The Impact of Poaching on Kenya's National Security: 2006 – 2019. Available at <https://shorturl.at/ekpzB > Accessed on 10th October 2023.
[12] UN Chronicle. Available at < http://tinyurl.com/mtn8jwsh >Accessed on 10th October 2023.
[13] Billow Kerrow, 'How grand corruption in the counties undermines devolution' The Standard. Available at < https://shorturl.at/wEGZ1 > Accessed 21st November 2023.
[14] Illicit Financial Flows from Developing Countries: Measuring OECD Responses

1.1 Understanding Illicit Financial Flows (IFF)



In its nature, IFFs entail the ingenious ways that finances leave a country undetected usually through illegal activities like tax evasion, corruption, or money laundering.[15] These activities move money out of a country secretly, which in turn harms the country's economy and its ability to provide essential services to its citizens. Conversely, other definitions have put emphasis on the origin of the funds, that is, if the funds are in violation of laws in their origin, or during their movement or use, are therefore considered illicit, for instance, the 2016 Report of the African Union High-Level Panel on Illicit Financial Flows from Africa defined IFFs as money illegally earned, transferred or used.[16] Given that Kenya's governance system is based on a devolved system, illegality across any stages of such outflows does not nullify the intent and purpose of such outflows, which is to hide funds. Though broad, this definition encompasses all forms and enablers of IFFs. Further, it also avoids the complicated debates of what qualifies as IFF by covering the entire breadth of financial transactions.[17]

1.2 Domestic Resource Mobilization (DRM)

DRM is the process of collecting funds from sources like taxes, investments, and savings within the country itself to fund various projects and government activities. For example, IFFs through trade misinvoicing significantly reduces DRM in developing countries compared to developed countries which rely on income taxes as revenue sources.[18] This loss of funds from developing countries greatly impairs domestic resource collection, further reducing the quality of services provided. Some governments in developing countries have opted for government incentives to encourage foreign direct investors (FDIs) to invest in specific sectors. These incentives are typically designed to reduce the financial burden on businesses and provide them with various benefits to stimulate economic activity.

These governments might issue incentives packaged as Free Trade Zones (FTZ) or special economic zones. These zones are set up within a country and have more favorable

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[14] Illicit Financial Flows from Developing Countries: Measuring OECD Responses

[15] Global Financial Integrity. Available at <http://tinyurl.com/84ruaheu> Accessed on 21st November 2023.

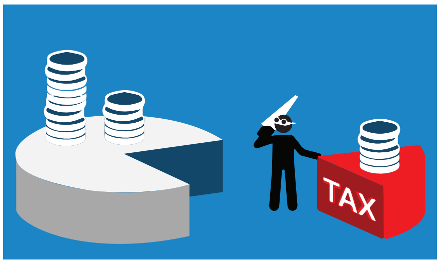
[16] Report of the High Level Panel on Illicit Financial Flows from Africa. Available at <https://shorturl.at/lmtBU> Accessed on 10th October 2023.

[17] Report of the High Level Panel on Illicit Financial Flows from Africa. Available at <https://shorturl.at/lmtBU> Accessed on 10th October 2023.

[18] Stopping Illicit Financial Flows Across Borders: The Case of Trade Misinvoicing. Available at <https://shorturl.at/ozCMP > Accessed on 21st November 2023.

economic conditions that aim to attract local and foreign investors. Despite these incentives for investments being beneficial, they carry risks that include loss of revenue due to tax incentives and trader interest to acquire cheaper rates for themselves. Further, a report done by the Organisation for Economic Co-operation and Development (OECD) in 2018, stated "...illicit trade, and other forms of criminality, such as fraud and money laundering, are relying on the opaque nature of FTZs to further the interest of bad actors, by allowing them to carry out illicit business, at lower risk."[19]

1.3 Legal Framework for Devolution in Kenya



Devolved system of governance in Kenya was birthed from the demand for a decentralized system of governance. This push was accelerated by the demand for equitable distribution of national resources, platform for economic and social development and informed decision making through public participation.[20] The devolved system aimed to be a vehicle of inclusive development in the political, social, and economic spheres.

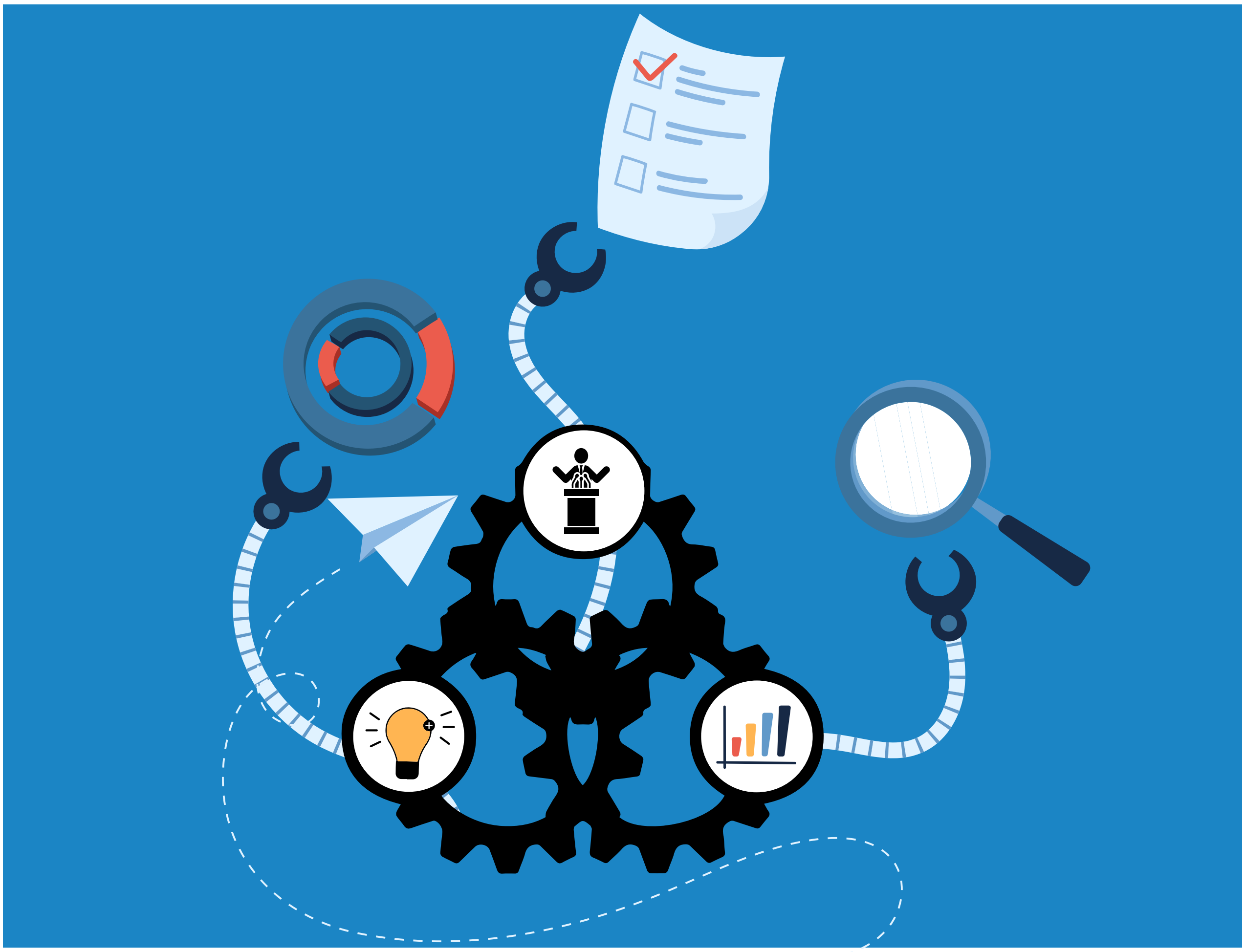
The devolved system of government is anchored in Kenya's 2010 constitution which establishes 47 counties and delineates the functions of the counties, fiscal powers, and governance structures. To support devolution, other laws, such as the Intergovernmental Relations Act, No. 2 of 2012, have been enacted to establish a framework for consultation and co-operation between the national and county governments and amongst county governments; to establish mechanisms for the resolution of intergovernmental disputes pursuant to Articles 6 and 189 of the Constitution, and for connected purposes.[21] Additionally, several institutions, including the Senate, Council of Governors (CoG), Intergovernmental Relations Technical Committee (IGRTC) and Intergovernmental Budget and Economic Council (IBEC)[22] were also set up to facilitate the operations, oversight and service delivery between the two levels of government. This report refers to them as shared institutions due to their nature of operation and mandate, as they form a critical link between counties and the national government.

[19] CRD Global 2023. Available at < https://shorturl.at/fhM16 >Accessed on 21st November 2023.
[20] Devolution in Kenya: The Good, the Bad and the Ugly. Available at< https://shorturl.at/uFNVX> Accessed on 21st November 2023.
[21] Kenya Law. < https://shorturl.at/dfuBQ> Accessed on 21st November 2023.
[22] No. 2 of 2012 Intergovernmental Relations ACT

2 | METHODOLOGY AND DATA

Despite the existing pieces of literature and evidence-based research on DRM and IFFs, this study adds value to these discussions by focusing on the Kenyan IFF laws and information results of a desk review of past literature and descriptive statistics of secondary data. Additionally, key informant interviews were undertaken to understand the effect of IFFs on DRM at the county level, and policy views on the need for shared institutions to take part in curbing IFFs were conducted. The scoping is segmented and organized around the national and international laws aimed at preventing IFFs from diverse sources.

The three pillars of opportunity, capability, and political that influence IFFs within a government are also taken into consideration in the scoping process because they have an impact on the parts of the government that determine the level of IFFs.[23]



[23] A Scoping Study of Illicit Financial Flows Impacting Uganda. Available at< https://shorturl.at/kpH36 > Accessed on 21st November 2023.

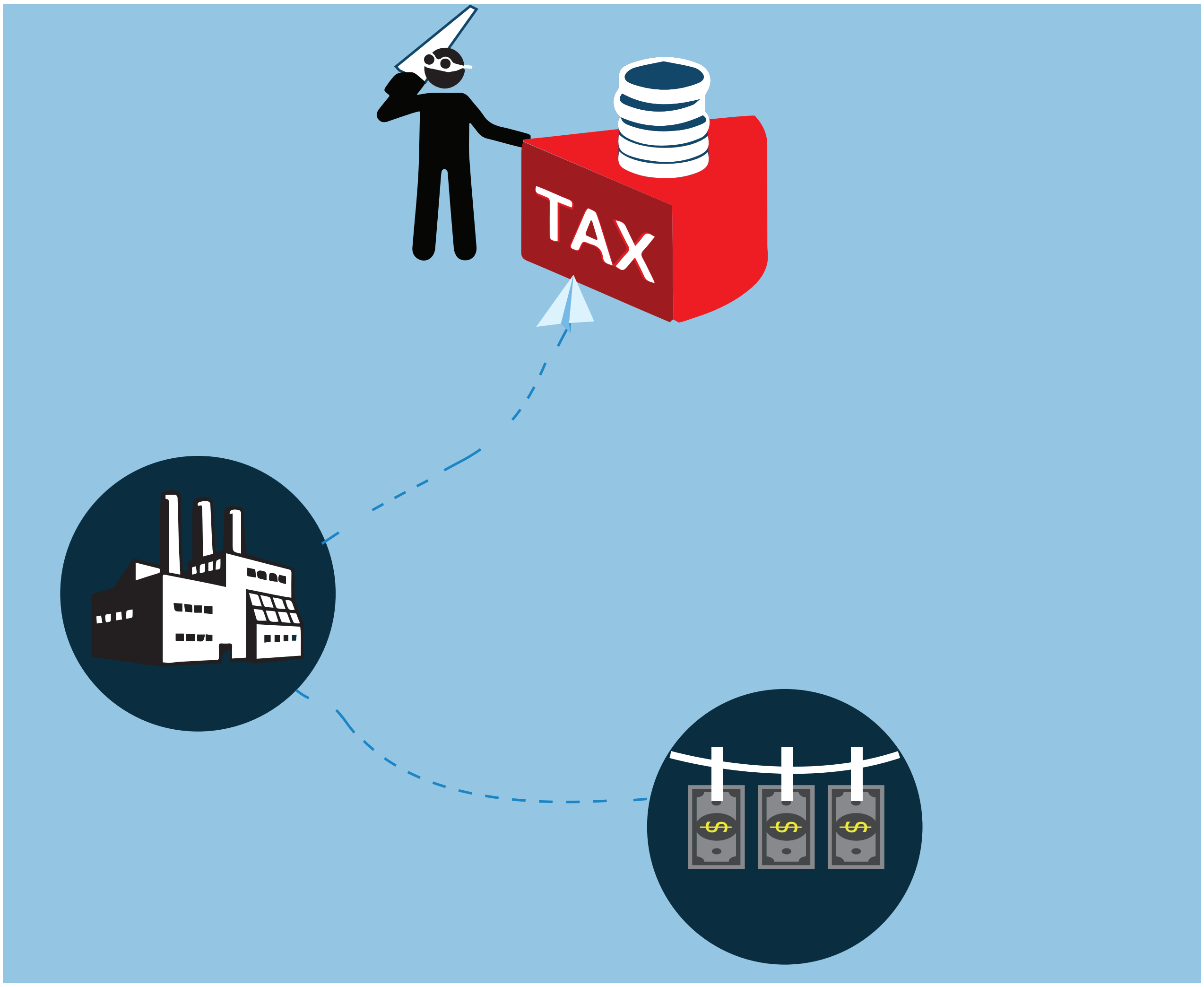
3 | SCOPE OF THE REPORT

To determine the scope of this report, we observed that the leakages that occur at county levels characterized by elements of IFFs have often been linked to corruption, with the proceeds circulating locally. Additionally, we also extensively discussed both the narrow and broad[24] definitions for IFFs as advanced by several reports and literature. This report adopts both definitions in the discussions advanced. Therefore, this report covers Kenya's IFF laws and existing information with a focus on the participation of counties in fighting IFFs. The report examines whether current laws address the actors' ultimate goal of hiding the proceeds away from the public eye and law enforcement agencies, given that IFFs are characterized by a number of enablers and driven by "push" and "pull" factors, with the desire to hide illicit wealth being the most obvious push factor driving IFFs. Further, the policy areas covered are to a larger extent determined by the availability of information and secondary data.

[24] The Effect of Illicit Financial Flows on Government Revenues in the West African Economic and Monetary Union Countries. Available at< http://tinyurl.com/59yxhpsb > Accessed on 21st November 2023.

4 | LINK BETWEEN IFFS AND RESOURCE MOBILIZATION

The interest attributable to the significant effects that IFFs have on the levels of development of different countries is almost equitable to the efforts[25] put to unpack the complex relation between IFFs and resource mobilization. The leakages through IFFs undermine public service expenditures and ultimately, the economic development in poor countries. Regarding the connection between IFFs and resource mobilisation, the latter is universally acknowledged in the literature to be a barrier to resource mobilization and wealth creation. In fact, empirical studies carried out in several African nations have shown that the burden of public debt would disappear if IFFs were stopped.[26]



[25] The Effect of Illicit Financial Flows on Government Revenues in the West African Economic and Monetary Union Countries. Available at< http://tinyurl.com/59yxhpsb > Accessed on 21st November 2023.

[26] Capital Flight from Africa Causes, Effects, and Policy Issues. Available at< http://tinyurl.com/3uwa6wky > Accessed on 21st November 2023.

5 | LEGAL AND REGULATORY ANALYSIS

The African High-Level Panel on Illicit Financial Flows defines IFFs as money illegally earned, transferred, or utilized.[27] The Global Financial Integrity defines IFFs as illegal movements of money or capital from one country to another.[28] The GFI definition underscores the need for the cross-border aspect of IFFs, which informs the subsequent analysis. This means that any transaction or crime involving cross-border movement of funds can be a source of IFFs. Looking at Kenya's legal framework for IFFs, they can generally be classified into three broad categories based on the sources of IFFs, namely:

- Commercial tax evasion, trade misinvoicing, and abusive transfer pricing;
- Criminal activities, including the drug trade, human trafficking, illegal arms dealing, and smuggling of contraband; and
- Bribery and theft by corrupt government officials.

The above categories are not exclusive but are only meant for effective discussion since, for example, crimes such as tax evasion may still be classified as originating from criminal activities in the second option. Similarly, corruption may cut across the categories especially as an enabler. From the diverse sources of IFFs, there is no global or national statute dedicated explicitly to addressing IFFs. However, there are several national and international laws aimed at preventing IFFs from diverse sources, which will be discussed below.

[26] Capital Flight from Africa Causes, Effects, and Policy Issues. Available at< http://tinyurl.com/3uwa6wky > Accessed on 21st November 2023.
[27] Report of the High Level Panel on Illicit Financial Flows from Africa. Available at <https://shorturl.at/lmtBU> Accessed on 10th October 2023.
[28] Global Financial Integrity, 'Illicit Financial Flows'. Available at. <http://tinyurl.com/84ruaheu> Accessed on 10th October 2023.

5.1 Tax-Related Sources of IFFs

There are several tax-related sources of IFFs, including commercial tax evasion, aggressive tax avoidance, trade misinvoicing, and abusive transfer pricing.[29] For a long time, there was no global effort to address tax-related sources of IFFs at the international level since countries relied mainly on bilateral and multilateral treaties. However, in the recent past, there have been efforts with leading bodies such as the Organization for Economic Cooperation and Development (OECD) to build consensus on key tax issues such as transfer pricing, digital taxation, among others, and have a shared international approach. For example, the OECD's Model Tax Convention on Income and Capital, adopted in 2017, is a model convention that aims to guide countries when entering into bilateral tax conventions. Its key focus is the removal of tax-related trade barriers to cross-border trade and investment. It also helps prevent tax evasion and avoidance and facilitates the effective resolution of problems that may arise with regard to double taxation treaties.

At the national level, Article 209 of the Constitution 2010 confers the power to impose taxes on national and county governments. The Constitution mandates the national government to collect taxes, namely, income tax[30], value-added tax[31], customs duties, and other duties on import and export goods[32] and excise tax.[33] In imposing these taxes, the national government has adopted comprehensive statutes to define the rate and tax base of every tax, and the annual Finance Acts often amend the rate of taxes and the tax base. The taxation mandate of the county government is limited to property rates, entertainment taxes, and any other that may be added through a statute. Apart from the tax, county governments levy user fees, some of which may be classified as taxes, especially where the fees collected are used to fund unrelated expenditures.[34]

At the national level, despite laws defining each tax's scope and elaborate dispute resolution measures,[35] taxes are not optimally collected. For example, in the 2022-2023 financial year, the Kenya Revenue Authority missed its target by Kshs. 107 billion.[36] Tax evasion and avoidance, abusive transfer pricing, trade misinvoicing, and granting of generous tax incentives without effective cost-benefit analysis continue to significantly contribute to tax-related IFFs. Below is a discussion of the legal framework of some of the sources.

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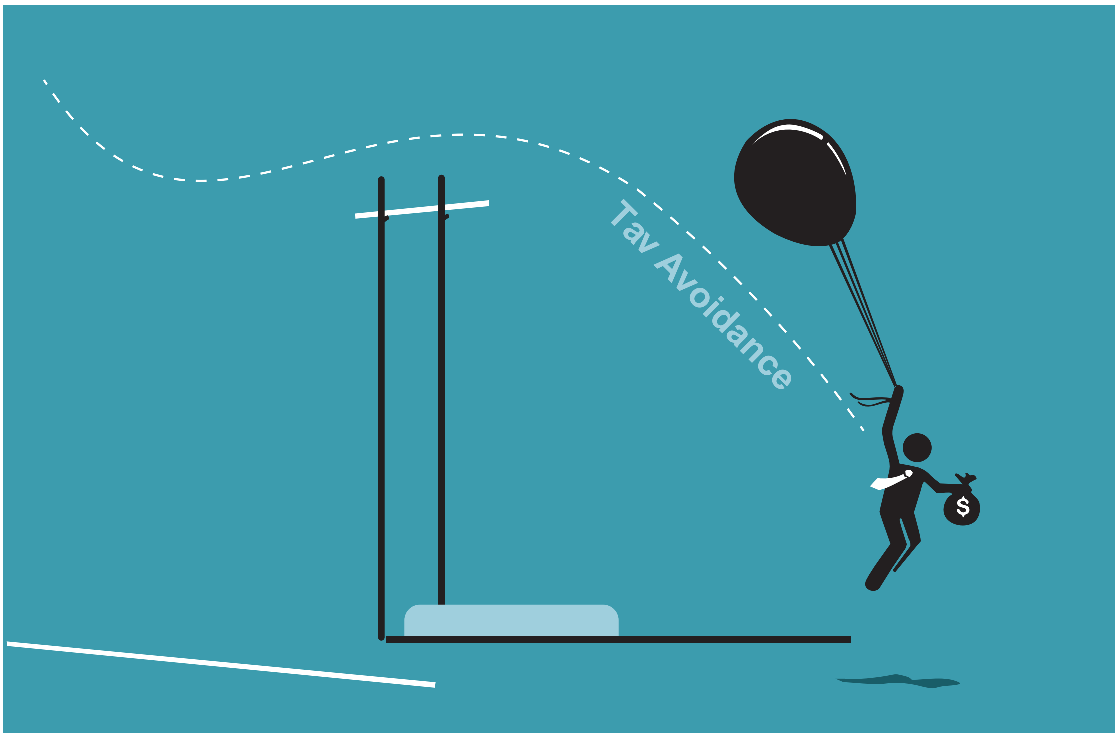
[29] Report of the High Level Panel on Illicit Financial Flows from Africa. Available at <https://shorturl.at/lmtBU> Accessed on 10th October 2023.
[30] The Income Tax Act No. 16 of 1973.
[31] The Value Added Tax Act No. 35 of 2013.
[32] East African Community (EAC) Customs Management Act of 2004
[33] The Excise Duty Act No. 23 of 2015.
[34] This happens where money collected from user fees such as single business permits are used by the county to fund other activities not related to the cleaning the towns and providing amenities such as sewerage systems, water etc. See Adam Smith 'Final Report: Own-Source Revenue Potential and Tax Gap Study of Kenya's County Governments' 17 Available at < https://shorturl.at/qzIJ9 > Accessed on 15th March 2022.
[35] For example, Tax Procedures Act of 2015
[36] Jacktone Lawi, 'KRA marginally misses target, collects Sh2.17tn in 2022/23' The Star July 14, 2023 available at < https://shorturl.at/mrvW2 > Accessed on 24th November 2023.

5.1.1 Tax Evasion And Tax Avoidance

Tax evasion occurs when one willfully breaks a tax law and fails to remit tax or remits a lower tax than what ought to be paid. This enables a taxpayer to escape tax liability resulting in losing tax revenue.[37] With this broad definition, tax evasion is a criminal offense and occurs when one fails to pay taxes in contravention of a statutory provision. Tax evasion may take different forms, including transfer pricing, trade misinvoicing, and fraud, some of which are subsequently discussed below.

The Tax Procedures Act 2015 defines tax avoidance as a transaction or a scheme designed to avoid liability to pay tax under any tax law.[38] Tax avoidance generally is not a crime, however, when done with a deliberate intention to unscrupulously evade taxes, also known as aggressive tax avoidance, it amounts to a criminal offence punishable under section 85 of the Tax Procedures Act. The taxpayer who sought to benefit from a tax avoidance scheme is punished by paying double the amount he would have otherwise avoided, while the agents who assist in creating schemes for taxpayers to avoid taxes are also punishable under section 92(c) of the Tax Procedures Act. Other initiatives, such as the introduction of turnover tax[39] and minimum tax[40] are part of the government's initiative to increase its tax base and seal loopholes for tax avoidance.



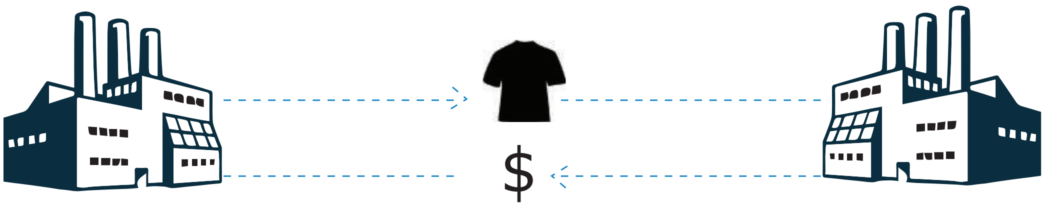
[37] Kenya Revenue Authority, 'Understanding Tax Evasion' Edition 001 available at < https://shorturl.at/fpGTW ; Kenya Revenue Authority, 'Tax Avoidance and Tax Evasion: A Tale of Two Errors', available at https://shorturl.at/hwBJ[4]> Accessed on 24th November 2023.
[38] Kenya Law. Available on < https://shorturl.at/adFV8 > Accessed on 24th November 2023.
[39] Income Tax Act Section 12C.
[40] Income Tax Act section 12D,

5.1.2 Abusive Transfer Pricing

This is a key source of IFFs in Kenya and Africa as a whole.[41] Transfer pricing is a practice that allows businesses owned by the same parent company or companies within the same multinational groups to buy and sell goods and services to each other. At first glance, there may not appear to be any issue with such transactions, however, they are often abused by related companies to affect the taxable profits of the different subsidiaries residence of different tax jurisdictions. For example, suppose the corporate income tax in country A is more than country B. In that case, transfer pricing may be used to minimise profits declared by subsidiaries in country A, thus reducing taxable income.

Section 18(3) of the Income Tax Act introduces the arm's length principle to guide transfer pricing by ensuring accurate application of the separate entity approach where a non-resident person carries out business with a resident or through a permanent establishment. Under the arm's length principle, it ensures that related firms' transactions are commensurate with the prevailing market rates. The [2013] Finance Act also sealed loopholes for transfer pricing by redefining ultimate parent to mean an entity that 'is resident in Kenya for tax purposes; is not controlled by another entity; and owns or controls a multinational enterprise group.' Further, to enhance country-by-country reporting, the resident constituent entities (not the ultimate parent entity) have been mandated to file country by country reports where the ultimate parent entity does not file in its tax jurisdictions, or in the event of systemic failure of the ultimate parent entity to file county by country reports in its jurisdiction of tax residency.[43]

Further, section 18(8) of the Income Tax Act gives the Cabinet Secretary for Finance power to issue guidelines for the determination of the arm's length value of a transaction. The Act also puts in place higher corporate tax rates for non-resident compared to residents because of the tax evasion risk that non-residents pose. However, the variation may be eliminated once the Kenya's Draft National Taxation Policy, which proposes standardization of corporate tax is adopted.[44] In addition, Kenya has the Income Tax (transfer pricing) Rules, 2006 to provide guidelines to be applied by related enterprises in determining the arm's length prices of goods and services in transactions involving them and to provide administrative regulations, including the types of records and documentation to be submitted to the Commissioner by a person involved in transfer pricing arrangements. These laws minimized base erosion and profit shifting, where multinationals shift profits to jurisdictions with low taxes even though the profits and significant business operations are based in other jurisdictions.



[41] Report of the High Level Panel on Illicit Financial Flows from Africa. Available at <https://shorturl.at/lmtBU> Accessed on 10th October 2023.
[42] Income Tax Act Section 18F.
[43] Income Tax Act Section 18D (9).
[44] The National Tax Policy June 2022 para. 3.7(i).

5.1.3 Trade Misinvoicing

Trade misinvoicing is also referred to as trade mispricing. It refers to the falsification of the price, quality and quantity values of traded goods for various purposes, some of which include evading taxes and in some cases, transferring value to another jurisdiction under trade-based money laundering.[45] In 2013, Global Financial Integrity estimated that Kenya lost US$908 million as a result of trade misinvoicing, which makes trade misinvoicing a significant source of IFFs from Kenya.[46] Trade misinvoicing results in losses in revenue from diverse sources such as value added tax (VAT), customs duty and income tax. To combat trade misinvoicing, Kenya has laws in place, such as the East African Community (EAC) Customs Management Act of 2004, that provides for cooperation, exchange of information, and common border controls for East African states[47] to aid prevention, investigation, and suppression of offenses such as tax fraud and evasion.

[45] Global Financial Integrity, Kenya: Potential Revenue Losses Associated with Trade Misinvoicing, October 2018. Available at < https://shorturl.at/tALR5 > Accessed on 10th October 2023.
[46] Ibid page 19.
[47] East African Community (EAC) Customs Management Act of 2004, Section 10.

5.1.4 Tax Incentives for Investments

The Africa High-Level Panel Report earmarked generous tax incentives as a key source of IFFs.[48] Tax incentives generally entail granting tax holidays, investment allowances, tax rate reductions and use administrative discretion in order to attract foreign direct investment. It is worth noting that tax incentives may not always negatively impact DRM or contribute to IFFs. However, they can often be abused, thus facilitating IFFs. This mainly occurs in cases where there is no cost-benefit analysis and opaqueness in granting the incentives. For a long time, Kenya did not keep records of revenue foregone (tax expenditure) due to tax incentives despite having a clear legal framework.

Article 210 of the Constitution 2010 provides that the imposition and waiver of taxes shall only be done via legislation. Amplifying this provision is section 77 of the Public Finance Management Act No. 18 of 2012 (PFM Act), which grants the Cabinet Secretary for Finance power to waive taxes, and records and reasons for the waiver must be reported. Equally, the waivers should only be authorised by statute. Further, to enhance the transparency of all incentives granted, section 82 of the PFM Act mandates the Kenya Revenue Authority to file reports of waivers/incentives granted each year, including the details of beneficiaries. Importantly, the provision mandates such data to be published and publicised.

Despite having robust provisions on incentives, there has not been consistent reporting from the government on revenue foregone as a result of tax incentives granted. The government started publishing tax expenditure reports in 2021[49] and subsequently, it publishes the tax expenditure reports annually.[50] The 2022 report indicated an increase

in tax expenditure to Kshs 393.6 billion (2.94 percent of GDP), from Kshs 292.9 billion (2.44%) percent of GDP) in 2021.[51] This increase comes with the need for greater transparency and accountability to ensure there are commensurate benefits from the tax expenditure. However, the reports lack comprehensive and aggregated data on tax

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[48] Report of the High Level Panel on Illicit Financial Flows from Africa. Available at <https://shorturl.at/lmtBU> Accessed on 10th October 2023.
[49] The National Treasury and Planning 2021, Tax Expenditure Report, September 2021. Available at <http://tinyurl.com/26vn6kmp> Accessed on 10th October 2023.
[50] See the 2021, and 2022 Tax Expenditure Reports.
[51] Tax Expenditure Report 2023 pg. (viii).

expenditure. For example, the reports do not include revenue foregone as a result of generous tax incentives granted to sectors such as Special Economic Zones and Export Processing Zones that enjoy a preferential tax regime.[52] The report indicated that preferential tax regimes like SEZ and EPZ were used as benchmarks and, therefore, not included as part of the tax expenditure. Further, the incentives were not subjected to scrutiny through cost-benefit analyses.

Other forms of tax incentives include entering into double taxation treaties with countries granting companies and nationals from other countries favorable tax rates on a reciprocal basis. Though the reciprocal approach makes the agreements appear fair to both countries, it confers more benefits to countries with increased trade. Kenya has double taxation agreements with several countries. However, the process is not always open and in strict compliance with statutes such as the Statutory Instruments Act 2013, the Treaty Making and Ratification Act No. 45 of 2012, and Article 10 of the Constitution. For example, in Tax Justice Network- Africa v Cabinet Secretary for National Treasury & 2 others (2019) eKLR, the high court declared a Double Taxation Agreement (DTA) with Mauritius unconstitutional for failure to undergo public participation under section 11 (4) of the Statutory Instruments Act 2013. In addition, though the government considered the agreement to be of benefit to the country, the government would have lost significant revenue, thus limiting its DRM ability given that Mauritius is generally a low tax jurisdiction and some of its firms have been linked to tax evasion syndicates in Kenya.[53] From the judgment, there have been a number of amendments to streamline the procedure for negotiation and adoption of DTAs and ensuring public participation. This amendments include amendment of Section 41 of the Income Tax Act to allow DTA to be negotiated under the Treaty Making and Ratification Act 2012 and not the Statutory Instruments Act.[54] Further, in April 2023, Treasury issued a proposals to parliament on the procedure of ratification of DTA's which allow public participation to happen at the negotiation stages since once the countries agree on a DTA, it becomes cumbersome to open up the negotiations to accommodate views from the public.[55]

Other ways in which tax incentives are abused include favoring the executive and cronies. For example, in the merger between Commercial Bank of Africa (CBA), in which the Kenyatta family has a stake, and NIC bank, the Kenyatta family benefited from a waiver of stamp duty that would have been approximately Kshs. 300 million.[56] This is an example of how tax incentives are granted without cogent justification. In some cases,

the corporate entities have successfully lobbied for the introduction of tax incentives in sectors such as the real estate sector, specifically affordable housing projects in their favor without cost-benefit analysis[57] thus reducing domestic resource mobilization.

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[52] Ibid.

[53] Will Fitzgibbon, 'Kenyan firm fined for elaborate tax evasion scheme routed through Mauritius' June 9, 2022, International Consortium of Investigative Journalists. Available at <http://tinyurl.com/38b5w55a> Accessed on 10th October 2023.

[54] Income Tax Act Cap. 470 Section 41.

[55] http://tinyurl.com/4e5khc67

[56] Edwin Okoth, 'NIC, CBA bank merger exempted from paying millions in share sale tax' August 18 2019 Business Daily Africa. Available at <http://tinyurl.com/j7mm7sn8 > Accessed on 10th October 2023.

5.2 IFFs from Criminal Activities

Criminal activities contribute significantly to IFFs in Kenya despite Kenya having a comprehensive legal framework to combat IFFs arising from acquisitive crimes. The legal framework includes the Narcotic Drugs and Psychotropic Substances (Control) Act, 1994; Prevention of Organized Crimes Act, 2010; Counter-Trafficking in Persons Act, 2010; Prevention of Terrorism Act, 2012 (POTA); Proceeds of Crime and Anti-Money Laundering Act (2009) (POCAMLA), Bribery Act, 2016, Wildlife Conservation and Management Act, 2013 (No. 47 of 2013), Anti-Corruption and Economic Crimes Act (ACECA) and the Penal Code. Some of the enablers include corruption, which accounts for a significant percentage of funds leaving the country and plays a facilitative role. For example, law enforcement officers like the National Police Service, one of the most corrupt institutions in Kenya,[58] are bribed to keep a blind eye to some of the transnational crimes. Also, money laundering channels enable criminals to disguise the origins of the proceeds of crime to make the proceeds appear to have originated from lawful sources.

To enforce the law, the government has established institutions such as the National Police Service, the Ethics and Anti-Corruption Commission, the Office of the Director of Public Prosecution, and the Assets Recovery Agency and even instituted a Multi-Agency Team consisting of all the relevant government agencies. Additionally, the judiciary adjudicates cases relating to crimes related to IFFs. In the Kenyan context, the judiciary established the Anti-Corruption and Economic Crimes Division in the High Court to specifically handle such cases. However, despite reporting cases of high-level drug trafficking like in the Akasha brothers case, these agencies did not prosecute them, and it was only after their extradition to the USA that they pleaded guilty to the charges of drug trafficking and related offenses.[59] Other challenges affecting the enforcement of criminal laws include the lack of effective witness and whistleblower protection in Kenya, especially after a spate of unexplained killings of key witnesses in high-profile cases.[60]

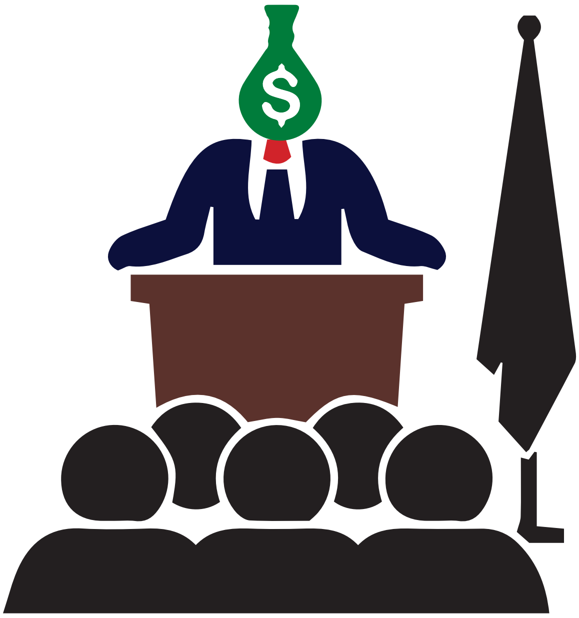
Increasingly, however, there has been progress regarding civil options such as non-conviction-based asset forfeiture aimed at confiscating proceeds of crime or unexplained wealth. From the precedent-setting case of Stanley Mombo Amuti v KACC [2019] Eklr, the Asset Recovery Agency and the EACC have successfully recovered significant proceeds of crime and unexplained wealth.[61] However, this process has not gone without questions, especially after the Court of Appeal overturned a decision by the High Court to forfeit

[57] Norad and Oxfam, 'Analysis of Tax Incentives and Exemptions in The Finance Acts from 2009 – 2019' December 2020. Available at <http://tinyurl.com/yeyyrvxc > Accessed on 10th October 2023.
[58] Sam Gituku, 'Police The Most Corrupt Department – EACC Survey Shows' December 31, 2022 Citizen Digital. Available at < https://shorturl.at/fuCQ2 > Accessed 22nd November 2023.
[59] The United Nations Office of Crime and Drug the Akasha brothers' international drug trafficking network
[60] Vincent Achuka, 'Gold Fraud: Death of Key witness leave prosecution on a tight spot' Daily Nation August 02 2021 Available at < https://shorturl.at/buzEK>; BBC News, 'Kenya 'ICC defense witness' in Ruto's trial killed' 6 January 2015. Available at < https://www.bbc.com/news/world-africa-30703876 > Accessed 22 November 2023.
[61] See Asset Recovery Agency, 'Forfeiture Judgements' available at < https://assetsrecovery.go.ke/case/forfeiture-judgements/ > Accessed 22 November 2023.

Kshs. 202 million belonging to the Deputy President Mr. Rigathi Gachagua that had been confiscated.[62] This case remains an issue of concern on the influence that politically exposed persons can have on active cases and their final determination. Other concerns also have emerged regarding asset management,[63] However, it is hoped that the Proceeds of Crime And Anti Money Laundering (Criminal Assets Recovery Fund) Regulations, 2023 recently promulgated, will address this concern. Also, where assets confiscated belong to a county government, for example stolen funds, the same should be returned to the county government seen in cases of immovable properties such as land.[64]
Other laws to complement criminal enforcement include the Companies Act 2015 and The Companies (Beneficial Ownership Information) (Amendment) Regulations, 2022, which aim to enhance corporate entities' transparency to enhance the investigation of criminal activities.

[62] Citizen TV Kenya, 'Deputy President Gachagua recovers Kshs 202M forfeited to State'. Available at <https://www.youtube.com/watch?v=SIQu4HbbIKs > Accessed 22 November 2023.
[63] Nairobi Anti-Corruption & Economic Crimes Division Civil Suit No. E002 of 2023 Asset Recovery Agency v Peter Oluwafemi Olaiwon (unreported).
[64] Dickens Wasonga, 'EACC hands over Sh410 million grabbed property to Kisumu county' 04 December 2023 The Star. Available at < http://tinyurl.com/4kcpmw7c >accessed 10/12/2023.

5.3 Bribery and Theft by Corrupt Government Officials



Bribery and corruption, mainly by government officials, remain another key source of IFFs in Kenya. To combat corruption among public officers, the Constitution 2010 dedicated Chapter 6 to leadership and integrity to ensure that public officials' character is beyond reproach. In addition, Kenya has statutes such as the Anti-Corruption and Economic Crimes Act, the Bribery Act, the Proceeds of Crime and Anti-Money Laundering Act among others, that define corruption-related offenses. However, convictions on cases of grand corruption are very few, often attributed to a lack of political will to prosecute corruption as most perpetrators enjoy political patronage. In other cases, inadequate investigation, lack of effective witness and whistleblower protection laws, and delays in courts resulting in backlogs and corruption in the law enforcement process all contribute to minimising the effects of anti-corruption measures. Some of the grand corruption scandals like Goldenberg, Anglo-leasing, and Euro-Bond, among others, remain unresolved despite evidence of the government losing huge amounts of revenue[65] which would otherwise be channeled to poverty alleviation programs. With the challenges of securing a criminal conviction, the Assets Recovery Agency and the EACC now use a civil option, non-conviction-based forfeiture, to recover proceeds of crime and unexplained wealth. However, the civil forfeiture option should not substitute criminal prosecution that plays a greater deterrence function.

With regard to recovery of assets transferred outside Kenya, the process is often riddled with complexities. For example, following a revelation in 2006 that proceeds of corruption were paid to an account owned by former Kenya Power and Lighting Chief Executive Officer CEO Samuel Gichuru and former minister Chris Okemo in New Jersey, the monies were only repatriated in 2022 following the signing of the Framework for the Return of Assets from Corruption and Crime to Kenya between the Kenyan Government and Jersey Island.[66] However, Kenya has laws such as the Mutual Legal Assistance Act, of 2011, and provisions of the POCAMLA[67] aimed at fostering international cooperation in tracing the

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[65] Wachira Maina, State Capture Inside Kenya's Inability to Fight Corruption, African Centre for Open Governance. Available at < https://africog.org/wp-content/uploads/2019/05/STATE-CAPTURE.pdf > Accessed 22 November 2023.

[66] Mark Lobel, 'Kenya to receive millions seized in Jersey to help fight Covid' BBC News 28 March 2022. Available at <https://www.bbc.com/news/world-africa-60377859> Accessed on 15th September 2023.

[67] See Part XII of the POCAMLA 2009.

proceeds of crime. Notably, even where conviction has been attained, some perpetrators appear to have been set free without clear reasons. For example, in July 2023, the president pardoned former Kenya Medical Research Institute director Davy Koech, who had been found guilty of three counts of fraudulent acquisition of public property and was fined Sh19.6 million or a six-year jail term.[68]

It is worth noting that Kenya has been able to put in place several measures to counter the IFFs, however as summarized below the agencies involved are to a greater extent, those under the national government;

[68] James Mbaka, 'Ruto pardons ex-Kemri boss Koech from 6-year jail term' 25 July 2023 The Star available at <http://tinyurl.com/4ap29sv7> Accessed 22 November 2023.

Measure	Purpose	Reference
Inter-Agency Anti-Illicit Trade Working Group	The group was launched in 2018 "to facilitate dialogue between government's law enforcement agencies, the private sector, consumer organizations and civil society to forge a joint action and collaboration against counterfeits and other forms of illegal commerce."	Inter-Agency Anti-Illicit Working Group Launched in Nairobi to Fight Trade in Counterfeits http://tinyurl.com/mujt79wv
National Action Plan to Combat Illicit Trade 2019-2022	The objective of the Action Plan is to combat illicit trade in "a synergized, coherent and collaborative manner." It recognizes that despite efforts from different government agencies, illicit trade thrives due to its complexity and evasive nature fueled by corruption and regulatory loopholes, and that a multi-agency approach would result in more effectiveness	State Department of Trade of the Republic of Kenya, National Action Plan and Implementation Framework to Combat Illicit Trade 2019-2022 http://tinyurl.com/2p85up35
Joint Border Committees	This is a platform where the Kenya Revenue Authority's Customs and Border Control Department, Partner Government Agencies, and the private sector convene with the "objective of trade facilitation and securing the border	Kenya Revenue Authority, Customs and Border Control Department (Nairobi: Kenya Revenue Authority, N.D) http://tinyurl.com/2rd6ajrd
National Baseline Survey on Counterfeit and other Forms of Illicit Trade in Kenya 2021	This study was conducted by the Anti Counterfeit Authority to highlight the extent of illicit trade in Kenya. Some key recommendations include legal and institutional reform to enhance information sharing among the Multi Agency Team on combating illicit trade; annual assessment of international trade-based level of illicit trade; training and recruitment of contributing government agencies; and the application of the National Observatory data submission platform for real time data submission	Anti-Counterfeit Authority, National Baseline Survey: Extent of Counterfeit and Other Forms of Illicit Trade in Kenya http://tinyurl.com/2799zsny
National Observatory on Illicit Trade Kenya	The Observatory is an online platform to allow government agencies and private sector actors to report illicit trade issues in real time and to inform policy and strategy for combating illicit trade	"National Observatory on Illicit Trade," National Observatory on Illicit Trade in Kenya http://tinyurl.com/4t4d8w8p

Source: *Trade-Based Money Laundering: A Global Challenge A policy memo by Global Financial Integrity, Fedesarrollo, Transparency International Kenya and ACODE January 2023*

6 | ILLICIT FINANCIAL FLOWS AND DEVOLUTION

Kenya adopted a devolved system of governance under the 2010 Constitution, and operationalised it in 2013. Kenya's domestic resource mobilization potential is an aggregate of the national government's revenue collection and the own source revenue collected from counties. At the county level, the key taxes collected are the property taxes and entertainment taxes.[69] Apart from these, a significant percentage of counties' own source revenue is collected from levying user fees such as cess, and market fees, among others.

Revenue leakages as a result of corruption and other crimes like fraud also apply to counties. With regard to revenue leakages from tax-related causes, counties experience this on a smaller scale when compared to the national. Property taxes that are classified as wealth tax are not optimally collected, therefore disproportionately favoring the rich. With regard to IFFs derived from criminal activities, though it is the national government that is tasked with enforcement of criminal laws, counties become victims of these crimes. For example, drug trafficking in Mombasa has seen the county spend significant revenue to rehabilitate drug addicts, which could be used to fund other poverty alleviation initiatives. Finally, county governments have also lost significant funds to corruption. Money from corruption in counties often finds its way outside the country mainly through purchasing high-end motor vehicles and funding education for children of senior county officials.[70]

Unlike the national government, which has comprehensive laws to define the scope of every tax, county governments have yet to develop specific laws for every tax.[71] For example, in collecting property taxes such as land rates, many counties rely on the Rating Act of 1963, which is largely outdated and often poses challenges in enforcing. While a few, such as Kiambu county have enacted the Kiambu County Valuation and Rating Act, 2016 to circumvent shortcomings that come with relying on the Rating Act of 1963. As a result, most counties have resorted to incentivizing landowners by granting periodic waivers of interest and penalties on land rates in order to pay the taxes which appear not to bear fruit. Also, though counties such as Kisumu, Nyeri, Kiambu and Nairobi have updated their valuation rolls, a significant number still rely on outdated valuation rolls that contribute to a low collection of land rates.[72] The resultant failure to optimally collect property taxes, which are predominantly wealth taxes, have seen massive revenue deficits in counties leading to the over taxation of low income earners like traders, boda bodas among others.

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[69] Constitution 2010 article 209.
[70] Paul Ogemba, 'Our money is clean: Daughters defend Okoth Obado in corruption case' The Standard 2022 < https://shorturl.at/ioEV2 > Accessed 22 November 2023.
[71] Adamsmith 'Final Report: Own-Source Revenue Potential and Tax Gap Study of Kenya's County Governments' Available at < https://shorturl.at/mzSWX > Accessed 15th March 2022.
[72] The National Treasury and Planning, National Policy to Support Enhancement of County Governments' Own-Source Revenue February, 2019 pg. 5; Nairobi County, 'Public Notice – Valuation Roll'. Available at <http://tinyurl.com/y3venm7r > Accessed on 22nd November 2023.

The preparation of a County Spatial Plan is a requirement under the County Government Act, 2012, which requires that all County Governments in Kenya prepare and implement Geographic Information System (GIS) – based County Spatial Plans. The Spatial Plan offers a broad vision for sustainable development within the county, for instance, it outlines major natural resources for proper utilization to benefit the county's residents, migration to digitized revenue collection, including the distribution of people and activities, within the context of efficient, productive and sustainable use of land and other county spaces[73] and help in growth of the County Government's annual revenue returns.

Despite being obligatory under the County Government Act of 2012 for counties to develop county spatial plans, ten years down the line, only six counties have approved comprehensive county spatial plans as a guideline for capital investment and monitoring and evaluation of targets set for usage of their resources. Though, weak technical knowledge, skills, and lack of effective tools and technologies have been sighted as a hindrance for effective formulation, implementation, monitoring and evaluation of spatial plans[74] , there is a need to speed up the process in order to ensure that optimal benefits are derived from the resources that fall within the counties as well as reduce pilferage through digitization of the revenue system.

[73] County Governance Toolkit. Available on <http://tinyurl.com/muy4s9km> Accessed on 22nd November 2023.
[74] Capacity Development on County Spatial Planning in Kenya. <http://tinyurl.com/3p8z27pp > Accessed on 22nd November 2023.

7 | SUMMARY OF FINDINGS

7.1 Legal and Regulatory Analysis

Kenya has a legal and institutional framework that supports the fight against IFFs. Though the mandate for mobilisation of resources for each level of government is well spelt, taxes are not optimally collected. Tax evasion and avoidance, abusive transfer pricing, trade misinvoicing, and grant of generous tax incentives without effective cost-benefit analysis continue to significantly contribute to tax-related IFFs. Further, the taxation mandate of the county government is limited and can only be added through a statute which entails lengthy legislative process. For instance, for a county to collect taxes in the mining sector, changes in the national level instruments like the Mining Bill have to be made. Most counties might not be able to lobby for such process to take place hence hampering collection of taxes from such sectors by counties.

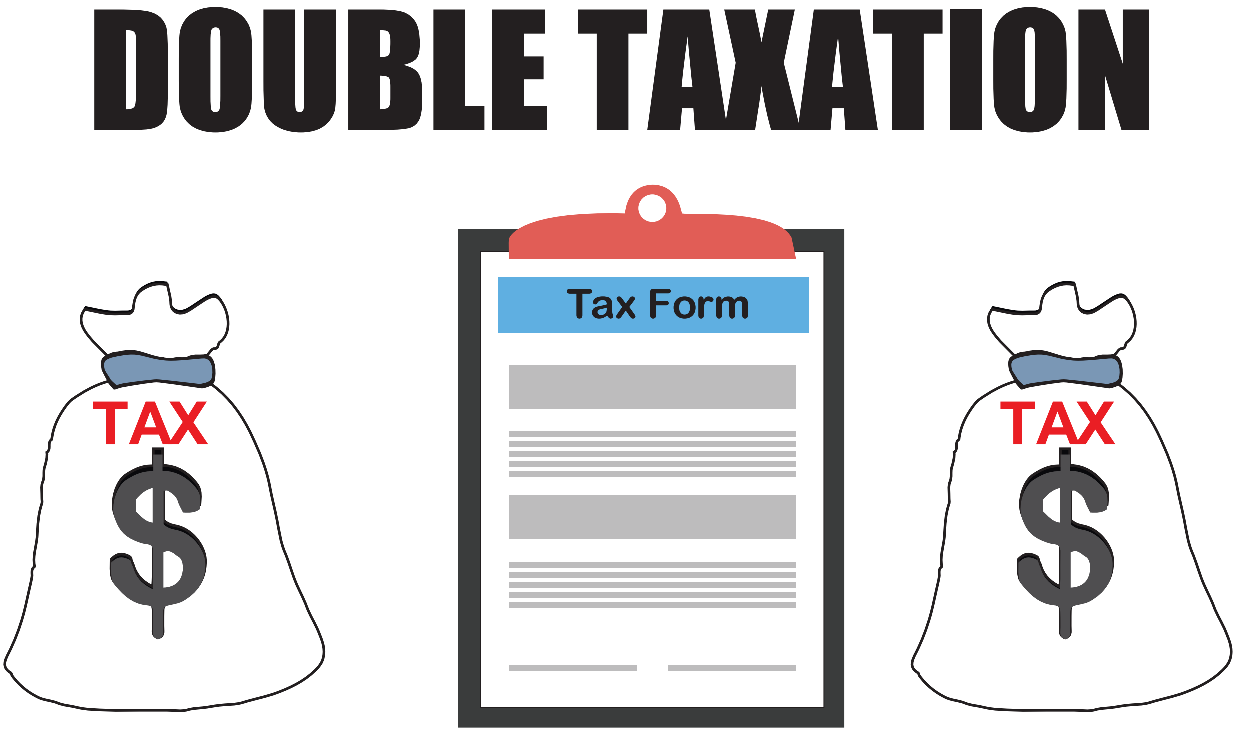
7.2 Tax Incentives for Investments

There has been a lack of consistency in reporting on revenue forgone as a result of tax incentives granted by the national and county government. The reports presented by the government so far fall short of including revenue foregone as a result of generous tax incentives granted to sectors such as Special Economic Zones and Export Processing Zones that enjoy preferential tax regime.[75]

[75] Ibid.

7.3 Transparency in Double Taxation Treaties

Kenya has double taxation agreements with several countries. However, the process has not always been open and in strict compliance with statutes such as the Statutory Instruments Act 2013 (previously)[76] and the Treaty Making and Ratification Act 2012. Such skewed treaties limit the country's DRM ability given that some of these jurisdictions are generally a low tax jurisdiction. In some cases, the corporate entities have successfully lobbied for the introduction of tax incentives in sectors such as the real estate sector, specifically affordable housing projects in their favour without cost-benefit analysis thus reducing domestic resource mobilization. It is hoped that DTAs will subsequently be entered as per the proposal by treasury submitted to parliament in April 2023 as the procedure allows room for public participation at the negotiation stage.[77]



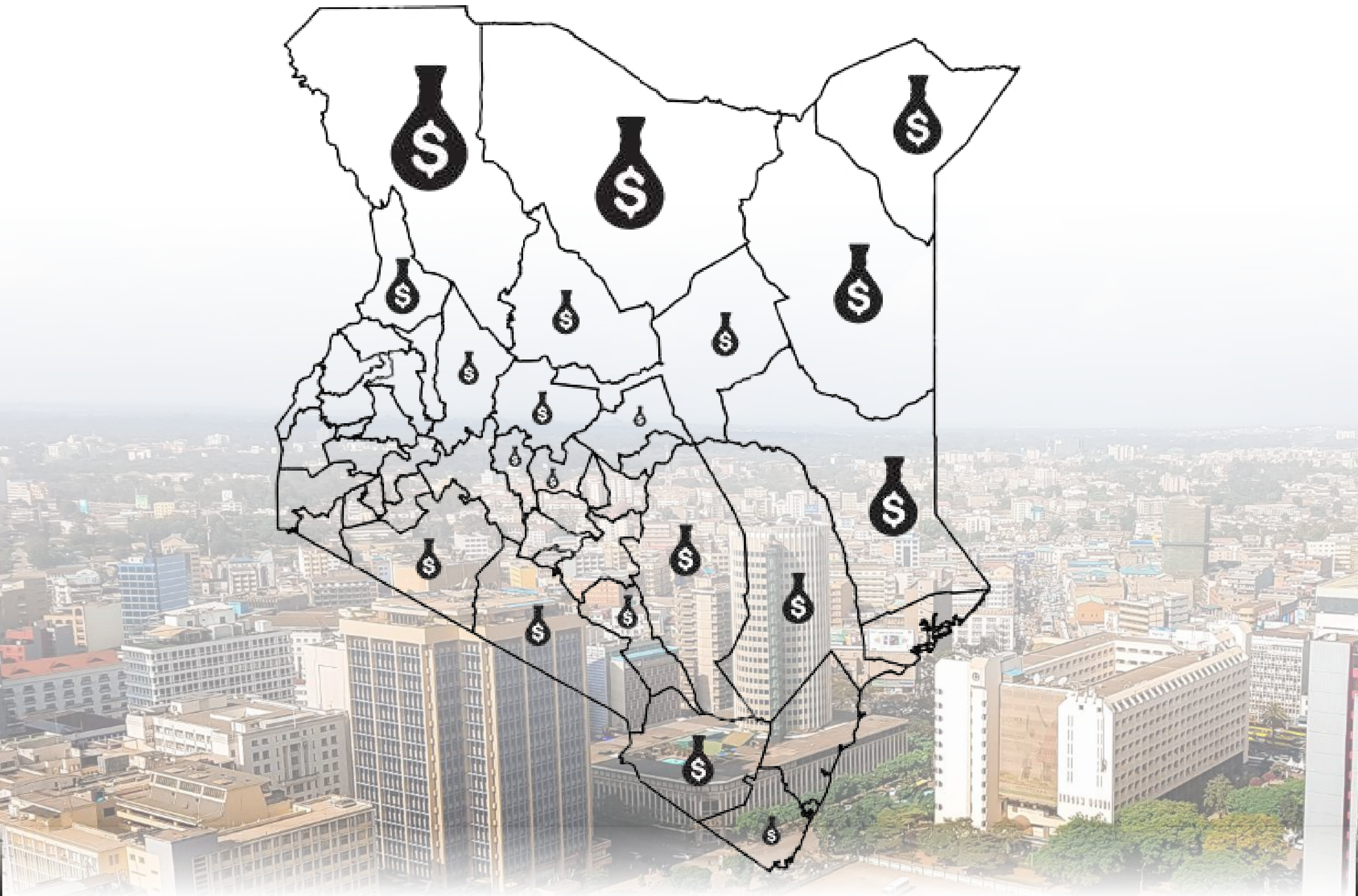
[76] See sec. 15 Finance Act 2021.
[77] Parliament of Kenya. Available on <http://tinyurl.com/4e5khc67> Accessed on 16th January, 2024

7.4 IFFs from Criminal Activities

Criminal activities contribute significantly to IFFs in Kenya despite Kenya's comprehensive legal framework to combat IFFs arising from acquisitive crimes. The key enablers include corruption, which accounts for a significant percentage of funds leaving the country and plays a facilitative role. This hinders the efforts channeled to improve resource mobilization at both levels of government.

7.5 Illicit Financial Flows and Devolution

When compared to national governments, counties experience revenue leakages from taxes related causes at a smaller scale. Property taxes that are classified as wealth tax are not optimally collected, therefore disproportionately favouring the rich. For IFF related activities, counties become victims of such crimes since they are not directly mandated to enforce any of the laws that fight against such related activities. Corruption, which is the main enabler of IFFs related activities at county level, has also left counties losing significant funds to corruption. Monies from corruption in counties have often found its way outside the country, mainly through purchasing high-end motor vehicles and funding education for children of senior county officials.[78]



[78] Paul Ogemba, 'Our money is clean: Daughters defend Okoth Obado in corruption case' The Standard 2022. Available on < https://shorturl.at/arOSY > Accessed on 22nd November 2023.

8 | RECOMMENDATIONS

The two levels of the Kenyan government continue to face difficulties in realizing their resource mobilization goals due to IFFs, as discussed in this report. Fighting IFFs should be a priority for both levels of government. Often, IFFs are symptoms of a serious governance problem and a broader range of governance issues that are faced by many governments. Building adaptable, efficient institutions and frameworks that guarantee seamless coordination between the two levels of government should be the ultimate goal of the objective to increase domestic resource mobilization and fight against IFFs.
The following are recommendations proposed by this report as ways to help reduce IFFs, strengthen domestic resource mobilization efforts, and ultimately increase domestic resource mobilization;

i. The county governments should be supported to develop legal policy frameworks that comprehensively define the scope of every tax. This will help improve and make it more efficient to mobilise own source revenue by the counties. It would further reduce the general incentivizing landowners through granting of waivers of interest and penalties on land rates.

ii. The county governments should be included in the inter-agency task forces created by the national government, Inter-Agency Anti-Illicit Trade Working Group, so as to have a comprehensive strategy for combating IFFs.

iii. The county governments should advance the development of the spatial plans to realize better resource management within the devolved governments. To overcome the shortcoming of resources that support generation of these plans, county governments can partner with civil society and other national government agencies that will offer them technical support.

iv. The anonymity of entities or companies enables many illegal activities, such as tax evasion, corruption, and money laundering to occur concealed from some county governments'. Therefore, county governments should use the information available in beneficial ownership registries to increase transparency and effectiveness in the public procurement and public investment processes. This will ensure fair, equitable, transparent, competitive, and cost-effective spending. Beneficial ownership data can help prevent corruption and fraud by detecting actors trying to subvert the contracting procedure for personal gain.

v. To evaluate the current and future tax incentives, a cost-benefit analysis should be conducted jointly, between the two levels of government. Essentially, tax incentives should only be offered if the additional tax revenues anticipated in the long term can make up for taxes omitted in the short or medium term, or if quantifiable positive externalities can be found with an equivalent impact. Further, both governmental tiers should be involved in the creation and management of free trade zones, which have been identified as avenues for IFFs. This can be accomplished by ensuring transparency and public access to information, including contractual and operational procedures.

vi. A framework on how the national government engages counties in approval of waivers of taxes should be developed. This ensures that counties are included in decision making, especially for resources that they are custodians of or the introduction of tax incentives in sectors such as the real estate sector.

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