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INTERNATIONAL TRADE AND CAPITAL FLIGHT FROM AFRICA: CHALLENGES FOR GOVERNANCE

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By Melvin D. Ayogu
University of Cape Town &
Mapungubwe Institute for Strategic Reflection,
Johannesburg, South Africa

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By Melvin D. Ayogu*

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* Adjunct Professor, Graduate School of Business, University of Cape Town & MISTRA Fellow, Mapungubwe Institute for Strategic Reflection, Johannesburg, South Africa. A grant from the Open Society Foundation through the Political Economy Research Institute (PERI), University of Massachusetts at Amherst, is gratefully acknowledged. Additional support from Freidrich Ebert Stiftung, Germany is acknowledged. Valuable research assistance by Damilola Adeniran of Center for Public Policy Alternatives (CPPA) Lagos is acknowledged as is administrative support by Blessing Obiedere (CPPA) for the Nigeria component of the study. This research has benefitted from comments and guidance by industry experts and practitioners as well as collaborators on the project especially editorial review by Jim Boyce and Leonce Ndikumana which has led to substantial improvement in focus and clarity. Special gratitude to Frank Edozie (Neconde Energy), Segun Omidele, Peter Owoeye (Bay Royal International), Peter Oriaifo (Erin Energy), Chris Arima (Neconde Energy), Leonard Ochueje (Central Bank of Nigeria), Obiora Madu (African Center for Supply Chain), Peter Onyia (Nigerian Customs), and Osita Mosanya (Nigerian Customs) for their valuable contributions. All errors and omissions are my responsibility and do not reflect the views of either the persons or institutions mentioned.

Preface to the Working Paper Series on Capital Flight from Africa

Capital flight constitutes a major constraint to Africa's efforts to fill the large and growing financing gaps that hold back its progress towards achieving sustainable development goals. The mounting evidence on the unrecorded outflows of capital from Africa has spurred calls for strategies to curb the financial hemorrhage that is afflicting the continent.

The existing evidence is still inadequate, however, on four fronts. First, the quantitative evidence is predominantly aggregate and does not furnish adequate country-specific information on the mechanisms of capital flight, its institutional contexts, and the role of domestic and foreign players in facilitating it. Second, the literature has not paid adequate attention to the destinations of wealth accumulated through capital flight and the roles of the banking sector and public institutions in destination jurisdictions. Third, much of the literature conflates the capital flight with the broader concept of illicit financial flows. While all capital flight is illicit owing to its unrecorded transfer – and often, as well, by virtue of the illegal origins of the wealth, and the failure to declare the assets and pay tax on the associated income – not all illicit financial flows are capital flight; for example, payments for smuggled imports are an illicit flow but distinct from capital flight. Fourth, the existing literature has not sufficiently explored the two-way relationship between capital flight and governance in national and international institutions.

To help fill these gaps in the literature, the African Development Policy Program at the Political Economy Research Institute has initiated detailed analyses in a project generously supported by the Open Society Foundations and the Friedrich Ebert Foundation. This Working Paper series presents the project's outputs. Our goal in issuing these reports is to engender informed public participation in decision making on financial regulation. Key findings will be distilled and published in the coming year in an edited volume that is forthcoming from Oxford University Press.

Léonce Ndikumana
Director, African Development Policy Program
University of Massachusetts Amherst

List of Acronyms

AML	Anti-money laundering
API	American Petroleum Institute
B/L	bill of lading
BoP	Balance of Payments
CEO	Chief Executive Officer
CIU	Customs Inspection Unit
COD	Country of Destination
COMD	Crude Oil Marketing Department
COO	Country of Origin
CPC	Customs Processing Center
DPR	Department of Petroleum Resources
DTI	Data Transmitting Interface
EFCC	Economic and Financial Crimes Commission
EIR	Equipment Interchange Report
FPSO	Floating Production, storage and offtake platform
FT	Financial Times
IMF	International Monetary Fund
IMTS	International Merchandise Trade Statistics
IOC	Independent oil company
IP	Intellectual property
KYC	know-your-customer
NCS	Nigerian Customs Service
NEPC	Nigerian Enterprises Promotion Commission
NIMASA	Nigerian Maritime and Safety Administration Agency
NNPC	Nigerian National Oil Corporation
NPDC	Nigerian Pipeline Development Corporation
POS	point of sale
PwC	PricewaterhouseCoopers
PAAR	Pre-Arrival Assessment Report
SADC	South African Development Community
SGD	Single Goods Declaration
SITC	Standard International Trade Classification
TDO	Terminal Delivery Order
UN Comtrade	United Nations International Trade Statistics Database
UNCTADstat	United Nations Conference on Trade and Development Statistics

I. Introduction

Poor governance is a binding constraint in the fight against capital flight and other illicit financial flows from Africa. Capital flight, in turn, undermines the efficacy of foreign aid as a tool for development. To further the goal of combating capital flight, and thus to enhance aid effectiveness, this paper examines the double-edged role of governance. Because it can facilitate or deter capital flight, the question of how government wields its power is of critical importance.

This paper focuses specifically on the governance of international trade and trade-related financial transactions. It demonstrates that the sword of governance has been wielded to cut predominantly one way—to facilitate capital flight—in key African countries.

The paper argues that an important part of "getting governance right" is to redress existing practices in the management and oversight of international trade data that create wide scope for transgressors and institutionalized malpractices. The responsibility of governments for cross-border trade data quality and data transparency cannot be shirked. But because states and public officials are often complicit in illicit flows, the need for independent verification systems for trade and financial data cannot be overemphasized.

The economist Dani Rodrik has observed that the effects of policy reforms depend on the institutional context in which they are implemented. Experience has demonstrated, for instance, that trade liberalization policies "would not work if fiscal institutions were not in place to make up for lost trade revenue, capital markets did not allocate finance to expanding sectors, customs officials were not competent and honest enough…"[1] Similarly, foreign assistance will not work if public trustees can deftly commingle aid monies with domestic resources and then launder such monies in foreign jurisdictions where recovery of stolen public assets is extremely costly to pursue.

Institutions can be defined as the complex chemistry of formal rules, informal rules and enforcement characteristics that together form a society's incentive structure.[2] A society's incentive structure

[1] Rodrik, Dani (2006) "Goodbye Washington Consensus, Hello Washington Confusion? A Review of World Bank's Economic Growth in the 1990s: Learning from a Decade of Reforms,", p.977. *Journal of Economic Literature* 44: 973-987.
[2] North, Douglass C. (1991) "Institutions." *The Journal of Economic Perspectives*, *5*(1), 97-112; and (2002) "Institutions," *The IMF Institute Courier*, 4.

determines the manner in which people interact and the kinds of organizations which arise to seize opportunities created by the incentives. When the incentive structure encourages good governance, regimes become public-regarding. When it encourages poor governance, predation, lack of accountability and corruption thrive.

As an example of what can happen when institutions function perversely, *Vanguard,* a leading newspaper in Nigeria, reported in 2016 that the Federal Government was losing $775 million per year in foregone revenue from oil and gas cargoes "discharged at undesignated terminals." This amount would be equivalent to approximately 2.7 percent of the annual revenue of the Federal Government of Nigeria at the time. "Maritime experts," the report elaborated, "hold the opinion that all the Federal Government needed to do over the years to sustain collectable revenue inflow form transportation, berthing and cargo discharge of vessels was to enforce the policies that have been in existence for many years." Instead, some flout the rules with what one expert termed "impunity." [3] This raises an obvious question: why would a government in need of development resources deprive itself of revenue in circumstances that are ostensibly within its control?

This paper seeks to identify and understand how political, social, and economic arrangements (formal rules, norms/conventions) facilitate corruption in general, and capital flight in particular, among other ways by making it difficult to detect. The smoke and many mirrors of capital flight, and arguments from skeptics about whether it actually happens, have been most pronounced in connection with the commodities trade. Resolving controversies on this subject requires a better understanding of the rules of the game of international trade that shape this channel of capital flight and its tributaries.

Before delving further, a few remarks on institutions and the nexus of governance and capital flight are in order. Formal rules are created and enforced by political entities as part of the instruments of governance. Third-parties rely on governments to ensure that agreements, once struck, are subsequently honoured or enforced. Increasing specialization of economic activities and the attendant allocation of rights and responsibilities induce an additional set of complications.

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[3] "FG loses 775.2m dollars on oil, gas cargoes discharged in undesignated terminals," *Vanguard,* 24 May 2016. https://www.vanguardngr.com/2016/05/fg-loses-775-2m-dollars-oil-gas-cargoes-discharged-undesignated-terminals-2/, accessed on 24 September 2019.

As complex transactions – involving a variety of relationships, some personal and others impersonal, interacting across locations near, far, and remote – become a regular feature of trade, the development of equally complex enforcement mechanisms will be required. Already we can observe instances of this shift in the current approach to managing trade-related intellectual property (IP) rights. The evolution of rights management as a dominant business strategy, in contrast to the legalistic approach of granting exclusive rights to IP through patent, copyright, and trademark protection, has been driven by cost considerations, particularly the cost of enforcement. Capital flight and money laundering, too, involve complex transactions between a matrix of actors across the globe. In the criminal enterprise "value chain", depicted schematically in Figure 1, some of the personalities in the matrix often are known while others are unknown to some of the players.

Figure 1: The Money Laundering "Value" Proposition

Whereas third-party enforcement is the remit of government, what may be termed "first and second-party enforcements" are the norms of "appropriate behaviour" that constrain the conduct of the individual parties entering into a contract. Development of the appropriate norms is crucial because third-party enforcement is imperfect. This offers insight into why citizens can at times flagrantly disregard formal rules. From experience, they may have come to believe that they can, on average, get away with the violation because of the unreliable nature of the enforcement mechanisms. This also can help us to understand how insurgents can successfully wage a long-drawn out war of attrition on the state, sometimes laying to waste expensive and strategic infrastructure such as crude oil pipelines,

factories or refineries. A case in point is Nigeria, where the unrest in the Niger Delta has frustrated many foreign oil exploration and production companies. Shell has made a major divestiture, while new investors are now more interested in deep sea operations offshore that are better insulated from the turmoil on land.

In complex exchanges involving dense networks, with costly third-party verification and subject to opportunism and cheating, as is typical of illicit financial flows, trust is crucial in facilitating transactions. In some cases, both formal and informal enforcement mechanisms may be in play, while in others informal mechanisms alone suffice. The position of the state as a monopolist of legitimate violence implies an unequal distribution of coercive power in the enforcement realm. As a result, individuals or groups have an incentive to try to hijack the government in order to determine how the "third-party" component of enforcement is exercised. Such corruption of government through corrosion of institutions is the grit of this study. The cases discussed illustrate the pervasiveness of the phenomenon of debasement, and its crucial role in capital flight from Africa.

Consider, for instance, the following statement from the South African Revenue Service (SARS), whose responsibilities include "record-keeping, verification, publication and analysis of trade data:"[4]

> Country code ZN is described as "Origin of Goods is Unknown." For purposes of better understanding, this has been renamed to "Gold, Petroleum and Other" as over 95% of this bubble is made up of gold. Gold due to legacy rules is treated as a country. You will therefore not be able to determine where the exports are going to [sic] or the imports are coming from. The aim is to rectify this, for gold specifically, as part of moving to the general system.[5]

When a country whose number one traded commodity is gold has a rule (until recently, at least) that says we do not reveal movements in our international trade in gold, the temptations that such an arrangement presents to would-be transgressors is immense.

[4]SARS, available at www.sars.gov.za/clientsegment/customs-excise/trade-statistics, accessed on October 3, 2018.

[5] SARS, "Trade Statistics: Explanations and Notes," available at http://www.sars.gov.za/ClientSegments/Customs-Excise/Trade-Statistics/Pages/Explanations-and-Notes.aspx, accessed on 22 August 2019.

Another curious rule allows South Africa to export and import with itself as the same Country of Origin (COO) and same country of Destination (COD). These roundtrips create fertile ground for the concealment of illicit flows. In the corporate world, audits are used to verify sales figures in annual accounts and to ensure that they represent *bona fide* sales and not internal transfers. Disguising internal transfers as sales is akin to "cooking the books." Years ago, Al Dunlap, who at the time was the CEO of Sunbeam, was charged with accounting fraud by the U.S. Securities and Exchange Commission for booking phony sales of electric blankets. An astute financial journalist, who thought it odd that the sales of electric blankets would be spiking in summertime, revealed these were internal transfers calculated to inflate the company's ostensible performance under his leadership.[6]

Applied to international trade transactions, what are data users to make of the balance of trade figures of a country that buys and sells to itself and books those transactions as "international trade"? Why was the recording of gold exports in South Africa not in accordance with established rules applied to other products? The wide latitude allowed when it comes to such official record keeping creates opportunities that some predictably exploit.

Similarly, in studies based on aggregated data at national levels, underinvoicing of exports and overinvoicing imports accounts for a significant component of illicit cross-border flows.[7] This work has proven useful in drawing attention to a phenomenon that appears to be widespread in the sub-Saharan region, prompting increased research efforts aimed at drilling down to the level of product types in individual countries. The analysis of such disaggregated trade data can help in uncovering some of the ways and means of capital flight as well as the institutional characteristics that shape how the practice plays out in different contexts within the region.

The remainder of this paper is organized as follows. Section 2 examines the relevant literature and the main issues of contention. Although African countries are highly dependent on primary commodity exports for

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[6] John Byrne, "How Al Dunlap Self Destructed," 6 July, 1998, available at https://www.bloomberg.com/news/articles/1998-07-05/how-al-dunlap-self-destructed , accessed on 30 July 2019. See also Floyd Norris, "S.E.C. Accuses Former Sunbeam Official of Fraud," *New York Times,* 16 May 2001.

[7] Leonce Ndikumana, James K. Boyce and Ameth Solum Ndiaye (2015) "Capital Flight from Africa: Measurement and Drivers." In Ajayi and Ndikumana, L. (Eds.), *Capital Flight from Africa: Causes, Effects and Policy Issues*. Oxford, UK: Oxford University Press.

foreign exchange earnings, the nature of the commodities varies country to country, ranging from solid (i.e. non-fuel) minerals to fuel to tree crops. Important non-fuel minerals include gold, silver, platinum, diamond, tantalum, and tungsten. Fuels are comprised of oil and gas. Section 3 considers trade in cash crops and solid minerals. Section 4 focuses on oil and gas. Summary and concluding remarks follow in Section 5.

II. Asymmetries in Trade Data

Estimates of trade-related capital flight from Africa[8] are based on the analysis of several internationally recognized conventional data sources, such as the Direction of Trade Statistics, the UN Comtrade, UNCTADstat, and the Balance of Payments accounts (BoP). The Direction of Trade Statistics is a database of the International Monetary Fund (IMF) that reports total imports and exports disaggregated by partner countries but not by product. UN Comtrade is the United Nations International Trade Statistics database. It contains detailed records both by product types and partner countries of imports and exports of goods crossing national borders, as reported by national statistical authorities, and "is considered to be the most comprehensive trade database available with more than 3 billion records."[9] UNCTADstat is a trade and development database that UNCTAD compiles, validates and processes based on a wide range of data collected from national and international sources.[10] The Balance of Payments (BoP) is a record of private and official transactions between the residents of a country and the rest of the world, including the exchange of goods and services as well as capital and unilateral transfers. The reporting format of BoP can vary across countries. Important BoP subaccounts are the current account (recording merchandise trade and services), the capital account (recording real and financial assets transactions), and the official settlements balance (recording foreign exchange transactions of the central bank).

These various databases enable trade misinvoicing to be estimated at the product level as well as at the aggregate level. A comparison is made between a country's recorded exports or imports to the imports

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[8] See, for example, Leonce Ndikumana, James K. Boyce and Ameth Solum Ndiaye (2015) Capital Flight from Africa: Measurement and Drivers. In Ajayi and Ndikumana, L. (Eds.), *Capital Flight from Africa: Causes, Effects and Policy Issues*. Oxford, UK: Oxford University; UNCTAD 2016.

[9] By United Nations, "About the data", available at https://comtrade.un.org/labs/dit-trade-vis/pages/about.html , accessed on 30 July 2019.

[10] For more, see "Statistics" available at https://unctad.org/en/Pages/statistics.aspx, accessed on 30 July 2019

or exports recorded by its trading partners, adjusting for the costs of freight and insurance. By aggregating across individual country-partners, a global estimate for the reference country can be obtained. A 2016 UNCTAD report views capital flight as largely responsible for the asymmetries in the Africa trade data.[11] This occurs when firms deliberately understate the value of their exports or overstate the value of their imports. In the case of exports, underinvoicing allows them to retain and conceal part of the foreign exchange earnings abroad; in the case of imports, overinvoicing allows them to remit foreign exchange overseas in excess of the actual cost of the imported goods, where the excess is retained and concealed from the country's authorities.

"Mirror data" refers to circumstances in which two entities collect information on the same transactions. In a mirror dataset, information from one source in theory duplicates the information from the other source. Bilateral trade data is one such example. Generally, any two trading partners are presumed to collect identical information on their trade in goods and services in any given period. By using this idea of correspondence of mirror data to examine trade on a bilateral basis, researchers have sought to gain insights into the discrepancies that in some instances have been so large and persistent that they cannot be plausibly attributed merely to data recording errors.

Cumulative discrepancies between mirror data in international trade lead to global asymmetries in bilateral trade statistics, a phenomenon that has been a subject of concern worldwide. The European Union has been particularly concerned about the discrepancies in intra-European trade in services (also known as "invisibles" because they do not involve physical goods).[12] The U.S. has been concerned with the sizable asymmetries in the bilateral merchandise trade data with China. Africa has been concerned about the large asymmetries in its primary commodities trade with the rest of the world. Aside from being concerned about its implications for capital flight, persistent asymmetries in mirror statistics calls into question the credibility of BoP statistics.

[11] Ndikumana, Leonce (2016) "Trade misinvoicing in primary commodities in developing countries: the cases of Chile, Cote d'Ivoire, Nigeria, South Africa and Zambia." Geneva: UNCTAD. Similarly, Ferrantino, Liu, and Wang (2012) conclude that capital flight explains a significant proportion of the asymmetries in the China-U.S. trade. Ferrantino, M. J., Liu, X., and Wang, Z., (2012) "Evasion behaviors of exporters and importers: Evidence from the US–China trade data discrepancy," *Journal of International Economics*, 86, 141-157.

[12] See for example Figueira, Maria-Helena, and Mushtaq Hussain (2006) "Asymmetries in EU current account data," *Working Paper and Studies 2006 Edition*, European Commission EUROSTAT, Luxembourg, November 2006.

The common framework for reporting on balance of payments transactions set out in the IMF's *Balance of Payments Manual* is intended to ensure conceptual and methodological consistency. Diligent application of the framework across countries restricts the range of plausible explanations for bilateral trade asymmetries by excluding basic methodological differences. Nonetheless, the uniform practices recommended in the IMF Manual are still open to a degree of variance in its interpretation and implementation. Such variations have generated competing hypotheses about the most likely explanations for the persistent methodical data asymmetries being recorded year after year.[13] These are discussed below, with examples of how some of the presumed factors play out in the African context.

Existing estimates of capital flight from Africa are likely to be conservative because of the near total absence of records on trade in services. Trade in services is a major component of foreign exchange movements because of the region's dependency on joint ventures in the extractive industries. These include engineering services, marine services, aviation, insurance and financial services, communications, computer and information services as well as royalties and license fees. Other missing items include miscellaneous business, professional and technical services, such as legal, accounting, management, consulting and public relations, advertising, market research, and research and development. As the African region strives towards its expressed goal of economic diversification, the services sector will come to occupy a larger niche overall. At present, most of these excluded services are provided by relatively highly-paid expatriates living in posh areas of the host countries often under tight security details. Yet the international trade in these services remains off the books.

The competing explanations for Africa's mirror-trade data asymmetries can be categorized into two major strands, namely the capital flight hypothesis and more innocuous alternatives. The latter strand maintains that asymmetries in mirror trade statistics are due to (a) non-deliberate shortcomings in the recording of trade transactions, (b) known and unknown diverse customs and practices at the primary sources where trading data are collected (metadata issues), and (c) habits that may appear to be

[13] For examples, see Figueira, Maria-Helena, and Mushtaq Hussain (2006) "Asymmetries in EU current account data," *Working Paper and Studies 2006 Edition*, European Commission EUROSTAT, Luxembourg, November 2006; Ferrantino, M. J., Liu, X., and Wang, Z., (2012) "Evasion behaviors of exporters and importers: Evidence from the US–China trade data discrepancy," *Journal of International Economics*, 86, 141-157; and Leonce Ndikumana and James K. Boyce, "Magnitude and Mechanisms of Capital Flight from Angola, Cote d'Ivoire, and South Africa," Amherst, MA: Political Economy Research Institute, Working Paper No. 478, December 2018.

deliberate obfuscation arrangements but in fact are simply administrative quirks. Various possibilities are outlined below.

Classification differences

On the innocuous end of the spectrum is the possibility that the same transaction may be reported accurately by both parties but classified differently. This would affect commodity-specific but not aggregate trade discrepancies. Several devices have been developed that function as conversion and correspondence tables to minimize such discrepancies at the product level reconciliation. The *Harmonized Commodity Description and Coding System* introduced by the World Customs Organization classifies trade by types. The *Standard International Trade Classification* (SITC) maintained by the United Nations Statistical Commission, now in its fourth revision, is designed to assist in classifying transactions. Its supplement, *Broad Economic Categories*, also produced by the UN, provides a 3-digit classification of transportable goods according to their main end use.

It is unlikely that primary commodities, which are Africa's predominant exports, are subject to this problem. The classifications of primary commodities are relatively clear cut. The items in question include crops such as cocoa beans, coffee beans, cut flowers, cashew nuts, and tobacco, and minerals such as diamonds, gold, silver, tantalum, tanzanite, platinum, crude oil and natural gas. These types of merchandise do not fall in grey areas because of their complexity or amorphous nature.

Classification of destination or origin countries also can lead to discrepancies in bilateral data comparisons. Again, these should not result in aggregate discrepancies. The UN manual on trade classification offers examples:

> The partner "Areas NES (not elsewhere specified)" is used (a) for low value trade and (b) if the partner designation was unknown to the country or if an error was made in the partner assignment. The reporting country does not send the UN details of the trading partner in these specific cases. Sometimes *reporters do this to protect company information… Due to confidentiality, countries may not report some of its detailed trade.* [Emphasis added.] For merchandise trade, this trade will - however - be included at the higher commodity level and in the total trade value for both goods and services.[14]

[14] UN, "About the data". Available at https://comtrade.un.org/labs/dit-trade-vis/pages/about.html, accessed on 1 August 2019

The timing of shipments can also lead to discrepancies: merchandise exported toward the end of one year may not be recorded as imports until the beginning of the next. If this were the sole reason for discrepancies, however, aggregation over several years would be expected to resolve the problem. It cannot explain asymmetries that persist over time or across products and partners.

Partner misattribution

Deliberate acts of false declaration of origin or destination by an importer or exporter or both parties can arise in order to benefit from trade policies, including duty reductions or tariff concessions, granted based on country of origin or destination. Misattribution can also facilitate smuggling or other forms of obfuscation that render difficult the task of asset tracing for purposes of freezing or confiscation of the proceeds of corruption and money laundering.

An interesting feature of the misattribution problem is that the rules of the game appear to have been shaped to give reporting authorities plausible deniability. Countries are granted considerable latitude on how to report transactions, notwithstanding the goal of harmonization. Expressing concern that the footloose criteria for partner attribution reduces the reliability of trade data, the UN Statistical Commission comments:

> For merchandise trade statistics, almost all countries report as partner country for imports the country of origin, which is determined by the *rules of origin established by each country* [emphasis added], and country of last known destination as the partner country for exports.[15]

Further complications arise from the transnational operations of multinational corporations engaged in global value chains.

Driven in part, perhaps, by recent controversies following the unsettling implications of studies relying on trade data,[16] the UN's International Merchandise Trade Statistics (IMTS) Expert Group has proposed that country of consignment be included in the data compilation manual as a possible partner

[15] UN, International Trade Statistics Knowledgebase, "Bilateral asymmetries." Available at https://unstats.un.org/unsd/tradekb/Knowledgebase/50657/Bilateral-asymmetries, accessed on 1 August 2019.

[16] E.g. UNCTAD 2016, Van Rensburg, Dewald (2016) "How wrong the UN was on SA gold smuggling," https://city-press.news24.com/Business/how-wrong-the-un-was-on-sa-gold-smuggling-20160729, accessed on 3 October 2019.

attribution.[17] The current rules allow the exporting country to record the country of consignment as the "last known destination." In conjunction with each country establishing its own rules of origin, this has created a wide berth for regimes so inclined to "cook their books" to do so with plausible deniability. Under the rules proposed by IMTS, the scope of plausible deniability is narrowed by specifying that a destination could in fact be a transit point rather than an importing country. This can be viewed as a strike against perfunctory reporting in the governance of international trade or as a tacit acknowledgment of a potential channel of illegitimate conduct in international trade. Either way, it represents a positive step. Current initiatives from UN Comtrade to upgrade its database to provide to users "more information on the nature of trade flows and partner-country attribution; symmetrical valuation of imports and exports and more information on insurance and freight costs; as well as more information on the nature of trade flows, especially re-exports, re-imports, and goods for processing, and intra-firm trade" also reflect efforts to improve the situation.[18]

Free ports

Free ports play an important role in anonymizing international trade analogous to that of anonymizers in the world of virtual currencies.[19] They make the task of trade data reconciliation more difficult, while increasing opportunities for trade-related capital flight. A free port is a place where imported goods can be held tariff-free pending (a) re-export, (b) duty-paid entry into the importing country, or (c) processed without customs duties prior to re-export. Existing free ports include the ports of Singapore, Hong Kong, Dubai, Panama and Amsterdam, the latter being Europe's leading entrepot. The business of importing goods for re-export, with or without any value-added in the free port itself, has grown enormously, particularly with the advent of containerization of cargoes. Indeed, the trade is now so well established that specialists have emerged. They double as both importers and exporters acting as dealers within certain shipping corridors. "Entrepot trade" as an established term in international commerce speaks to the importance of this activity (see Box 1).

[17] *Ibidem.*

[18] UN, "UN Comtrade upgrade plan 2018-2019". Available at https://comtrade.un.org/data/doc/UpgradePlan , accessed on 1 August 2019.

[19] U.S. Federal Bureau of Investigation (FBI), "Bitcoin Virtual Currency: Unique Features Present Distinct Challenges for Deterring Illicit Activity." Intelligence assessment, 24 April 2012. Available at https://www.wired.com/images_blogs/threatlevel/2012/05/Bitcoin-FBI.pdf, accessed on 3 October 2019.

Box 1: Free Ports as Trade-Anonymizers

What connects Bitcoins, entrepot trade, free ports and anonymizers? The answer, in a word, is *secrecy*.

Launched in 2009, Bitcoins are accounts (addresses) comprising unique strings of numbers and letters that represent units of the Bitcoin currency as well as uniquely identify the transactions. The transactions are not systematically linked to an entity. The "delink" feature endows it with some anonymity just as a free port would confer to the ultimate destination of a shipment, seen from the viewpoint of the country of origin.

Even though traded under some level of anonymity, Bitcoin transactions are nonetheless transparent, in that they are publicly available in a shared transactions register. Strictly speaking, therefore, Bitcoin is semi-anonymous as certain aspects of the transactions are not hidden. So are entrepot trades if the parties report truthfully, fully, and timely.

The anonymity of cryptocurrencies can be enhanced further by using accessories designed to camouflage the source of a Bitcoin transaction and hence facilitate a very high level of anonymity. With such devices, the digital footprints – the originator-sender's instructions to the end user-recipient – are completely obfuscated. These tools and services collectively referred to as "anonymizers" makes no pretensions as to their purpose.

Mixer, an advanced version of an anonymizer, obscures the chain of transactions on the blockchain (that is, on the up-to-date ledger containing encrypted records of the all the previous transactions) by bundling them in the same Bitcoin address and transmitting them together in a manner that conceals the origin of the transaction (i.e., it creates the impression that they were sent from another address than the true origin). Another piece of sophisticated software in this repertoire of anonymizers is a tumbler that executes remittance instructions through complex protocols defying attempts to uniquely map virtual coin addresses to specific transactions.

To those versed in the global practices of multinational corporations, these concealment mechanisms should be reminiscent of conduct of multinational corporations in the arena of commodity brokerage and secrecy jurisdictions. The analogy between Bitcoin and the role of free ports in Africa's commodity trade is evident.

When a country for various reasons is unable to trade directly with another foreign country, it is easy to see how entrepot trade can be a useful instrument. Say, for example, that Country A honors a regional sanction placed on country C, whereas country B is both a neutral party and an entrepot. Country A freely trades with B, and country C freely with B, as well. Then through the entrepot, A is enabled to trade with C indirectly and still maintain plausible deniability. If unchecked, entrepots can facilitate smuggling. Certificates of origin as well as declarations of destination can be forged by transgressors

operating within such facilities. Clearly, the reporting protocols in place in the free ports and the nature of their activities are important factors in resolving the challenges of trade data reliability and making inferences based on information in the trade data.

For instance, entrepot trade in the free port of Amsterdam may help to explain the Netherland's large and systematic trade discrepancies in cocoa beans from Côte d'Ivoire. In contrast to the direction of discrepancies with most of its other trading partners, Côte d'Ivoire's exports to the Netherlands exhibit inflated invoicing.[20] In other words, Côte d'Ivoire reports having sold more cocoa to the Netherlands than the latter reports importing. From the Ivorian perspective and in IMTS parlance, Netherlands is the country of "last known destination" of the beans from Abidjan. The Dutch story is particularly salient because trade in cocoa beans with the Netherlands accounts for over thirty percent of Ivorian trade in its most important commodity export.[21]

Trade in cocoa between Côte d'Ivoire and other trading partners apart from the Netherlands generally shows systematic underreporting , meaning that Côte d'Ivoire reports having sold less to those countries than their records acknowledge. This could be for purposes of capital flight. Or it could mean that the destination countries purchased some of the cocoa beans directly from Côte d'Ivoire and other quantities through third parties. Both practices are involved when the cocoa beans shipped to the entrepot are invoiced (and recorded in Côte d'Ivoire) at a below-market price and subsequently re-exported to their ultimate destination at their actual market price.

In attempting to unravel these discrepancies, French researcher Jean Merckaert finds that Netherlands does not provide UN Comtrade with the complete trade statistics on entrepot trade and nothing on cocoa re-exports specifically.[22] By choice, the Netherlands provides the UN with data on industrial exports and re-exports, but in an aggregated format that does not allow the components to be distinguished. This leaves to speculation as to why the country would provide the UN with data on industrial re-exports but

[20] See Ndikumana, Leonce (2016) "Trade misinvoicing in primary commodities in developing countries: the cases of Chile, Cote d'Ivoire, Nigeria, South Africa and Zambia." Geneva: UNCTAD, table 8.

[21]Aside from trade reconciliation, reliable facts about a country's direction of trade are an important variable in international economic relations and foreign policy.

[22] Jean Merckaert, "Bitter Chocolate: Capital Flight from Côte d'Ivoire." Amherst, MA: PERI Working Paper (forthcoming, 2019).

not primary re-exports, as well as why these data are reported only in aggregated format. In this, the Dutch are exercising their option within the parameters of IMTS 2010 convention. As previously noted, these sorts of anomalies in mirror data on trade are the focus of the current initiatives to upgrade the international reporting rules. At present, however, there seems to be sufficient latitude in the practice of entrepot trade for opportunistic persons readily to find ways to turn free ports into a staging ground for illicit trade-related activities. Therefore, these locations serve as potential enablers of illicit financial flows.

Another insidious consequence of the activities of trading hubs is noteworthy. By obscuring information along certain segments of the value chain—for example, hiding the price at which a commodity is traded or the location to which it has gone—the countries that harbor trading hubs effectively deny primary commodity-producing countries the opportunity to optimize their diversification profile. Developing countries need to know the path values associated with all the segments in the global value chain through which their primary commodities are processed. These are crucial parameters in the industrial strategies of countries seeking to determine the best segments of the value chain at which to locate, based on their dynamic comparative advantages. Developing those advantages where they do not yet exist is a core goal of development planning. It would not be rocket science for national authorities to enter into an international agreement on trade reporting that mandates greater transparency.

The ethical conundrums of denying developing countries a clear view of global economic activities in which they have a significant stake are no different in the tree crops subsector as in the extractive industries subsector. Correspondingly, it can be argued that the same gusto with which concerned global citizens have pursued the "publish what you pay" initiatives in the extractive industries, including the efforts under the Extractive Industries Transparency Initiative, should be applied to tree crops as well.[23] Perhaps such an initiative could be called "Publish What You Take," or better yet, "Publish What You Take and Where it Goes."

[23] "Publish What You Pay" refers to initiatives that address the lack of transparency in transactions in primary commodities, particularly those vested in the state such as fuel minerals and solid minerals. The generally low degree of transparency in such dealings facilitates exploitation and theft of public resources by private entities and public officials.

Smuggling

Import smuggling leads to discrepancies in trade statistics when the value of the merchandise is recorded in the data of the exporting country but is unrecorded or undervalued in the data of the importing country. "Pure smuggling" refers to cases where goods escape recording altogether. "Technical smuggling" refers to cases where the importation is recorded but with understated quantities, prices, or both. The primary motive for both types of smuggling is to evade import duties or other trade restrictions.

Of course, smuggled goods must be paid for in full, just like any other imports. Payments for these goods are one type of illicit financial flow. They are distinct from capital flight, another subset of illicit financial flows, in that the funds are used to pay for imports rather than stashed abroad. In balance-of-payments terminology, payments for smuggled imports belong in the current account whereas capital flight belongs in the capital account.[24]

Export smuggling likewise leads to discrepancies when the (full) value of the merchandise is recorded in the official books of the importing country but not the exporting country. Again, the primary motive is to evade duties or other restrictions on trade. It is generally less prevalent than import smuggling for the simple reason that taxes on exports are less common than taxes on imports. Unlike import smuggling, export smuggling also can be a conduit for capital flight if the earnings are held abroad.

Smuggling, both pure and technical, can occur at both ends of the exchange link.[25] Holding all else constant, if country A's border is relatively more tightly policed than country B's border, discrepancies in mirror trade statistics can be used to gauge the extent of smuggling into or out of country B. Differences in enforcement levels reflect differences in institutions. Using partner data as a benchmark

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[24] Note that the direction of import discrepancies due to smuggling is the opposite of those due to import under-invoicing for purposes of capital flight. The two offset each other and trading partner data comparisons can only tell us their net effect. In the measurement of capital flight, adjustments for import misinvoicing add to the BoP residual measure when under-invoicing exceeds smuggling and subtract from it when the reverse is true. For discussion, see Leonce Ndikumana and James K. Boyce, "Magnitude and Mechanisms of Capital Flight from Angola, Cote d'Ivoire, and South Africa." Amherst, MA: Political Economy Research Institute, Working Paper No. 478, December 2018.

[25] "Pure" smuggling refers to cases in which nothing is recorded by one or both trading partners. "Technical" smuggling refers to cases where import values (prices, quantities, or both) are understated in order to evade customs duties.

in estimating the extent of smuggling and capital flight from trade data is consistent with the presumption of better functioning institutions in partner jurisdictions, typically those in industrialized nations.[26]

There can be a linkage between smuggling activity and free ports. If a good is successfully smuggled into a free port, or if a smuggler can operate in both the source country and an entrepot jurisdiction, the merchandise can be more easily re-exported to a destination country in its clean transform, that is, as non-smuggled merchandise originating either from the free port or, per forged documentation, from any feasibly contrived origin of choice.

Misinvoicing

Misinvoicing refers to falsification of the value of a trade by deliberately misreporting the price, quantity, or both in trade documents. Besides smuggling, important motives for misinvoicing include tax evasion, tariff evasion, or to circumvent quota restrictions as well as foreign exchange controls. Other illegitimate purposes include enabling people to obtain money through false pretenses such as through false duty drawback, pre-financing of non-existent export trade and obtaining rebates for phantom exports (see Box 2).

When an exporter or importer falsifies documents in order to park money overseas illegally, the resulting capital flight fits within the meaning of money laundering as defined by U.S. anti-money laundering statutes.[27] The structuring of the movement of funds is designed to avoid detection (transaction reporting). The circumvention of exchange control regulations – in the case of exports, the requirement to surrender export proceeds to domestic monetary authorities at the official exchange rate, and in the case of imports, the procurement of foreign exchange at the official rate in excess of the true value of the imported goods – is itself a crime tantamount to tax evasion. In the destination country, the payments disguise the provenance of the wealth. So, in addition to the predicate crime of falsification, there is that element of structuring of a monetary transaction whose purpose is

[26] This proposition is taken up subsequently in the discussion of oil and gas export trade in Nigeria.

[27] U.S. Code § 1956, "Laundering of monetary instruments." Available at https://www.law.cornell.edu/uscode/text/18/1956.

Box 2: The Goldenberg Affair: Fraudulent Rebates for Phantom Exports

Africa's most infamous case of fraudulent manipulation of an export-incentive scheme was the "Goldenberg Affair" that roiled Kenya in the early 1990s. The details took 22 years to unravel, and seemed to touch everyone who was anybody in Kenyan politics and key institutions of governance. One of the scheme's masterminds was the chief of the country's secret police, James Kanyotu, whose formal title was the Director of National Intelligence for the 27-year period from 1965 to 1992.[28] Three hundred and fifty people were identified as the recipients of "Goldenberg money" totaling more than 150 billion Kenyan shillings (a sum roughly equivalent to US$1.5 billion).[29] In a country with a 2017 per capita income of 166,000 Kenyan shillings, this quantum was equivalent to the total average annual income of nearly one million Kenyans.[30]

Incorporated in July 1990 as a private limited liability company, Goldenberg International Limited, ostensibly began exporting gold and diamond jewelry under the Local Manufacturers (Export Compensation) protocol which provided for the payment by the Customs and Excise Department of 20 percent export compensation to eligible exporters on the value of goods exported. The company obtained an additional 15 percent payment on its exports of gold and diamond jewelry. It was a lucrative arrangement: as a National Public Radio report put it, "For every $100 of foreign exchange that Goldenberg brought in, the Kenyan government would kick in an additional $35 in Kenyan shillings - a huge bonus."[31] The monies were paid from Treasury and treated as customs refund.

Over time, Goldenberg International Limited and its collaborator, Exchange Bank Limited, were paid export compensation until about 1994 when the scheme was uncovered. Questions were then raised about the legitimacy of the scheme and payments, including the fundamental question of whether or not gold and diamonds were in fact exported by Goldenberg International Limited. Ultimately, it was determined that Goldenberg Affair was a case of subsidy for a phantom export.[32]

[28] Bosire (2005) "Report of the Judiciary Inquiry into the Goldenberg Affair," Republic of Kenya."
p. 25 et passim. Available at http://kenyalaw.org/kl/fileadmin/CommissionReports/Report-of-the-Judicial-Commission-of-Inquiry-into-the-Goldenberg-Affair.pdf, accessed 9 October 2019.

[29] *Ibidem.*

[30] Income per-capita is from Economic Survey (2018), Kenya National Bureau of Statistics.

[31] Julia Simon, "How One Of Kenya's Biggest Scammers Ended Up On The Ballot," National Public Radio, April 17, 2013. Transcript available at https://www.npr.org/2013/04/17/177650616/how-one-of-kenyas-biggest-scammers-ended-up-on-the-ballot, accessed 9 October 2019.

[32] Additional accounts can be found at http://www.kenyalaw.org/Downloads_FreeCases/93165.pd, accessed 1 May 2018.

concealment of the origin and nature of the money, or the nature of a trade to avoid transaction reporting. These are key elements in defining money laundering—*how one moves money and why.*[33]

For the scheme to work, the counterparty at the other end of the transaction must agree to park the payment per the request of its trading partner. Clearly, this cooperation is a necessary part of the structuring of the transaction. It is doubtful that the counterparty will declare in the know-your-customer (KYC) component of its banking documentation that the lodgment is the unremitted export proceeds or excess import payments placed overseas by its partner to evade foreign exchange controls.[34] If scholars of illicit financial flows can easily see through these machinations, it would be naïve to presume that those who cultivate such alliances and repeatedly participate in such schemes are unaware of the design and purpose of the schemes; namely, moving funds to impede detection by law enforcement, and helping to disguise these funds as legitimate wealth.

Similarly, it would be problematic to accept the notion that states serving as entrepots, free ports or shipping hubs are entirely oblivious of their role in enabling potentially illicit financial flows. On the contrary, it is reasonable to suppose that these jurisdictions are sufficiently savvy to understand the roles of trading hubs in aiding and abetting trade misinvoicing and misattribution. They also know how to eliminate such facilitations, if they so wish. In this respect, trading hubs are to international trade much as secrecy jurisdictions are to international finance. Both facilitate capital flight and money laundering. Their formal and informal rules work to attract this kind of activity by means of embedded incentives. The visible hands of government are on the table, spread openly for all to see and for self-interested parties to self-select.

Transfer pricing

Transfer pricing – more accurately, transfer mispricing – refers to purposive self-misinvoicing by multinational firms operating across multiple jurisdictions with the objective of "cooking the books" to relocate profits to low-tax (or no-tax) jurisdictions.[35] This phenomenon is distinct from capital flight.

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[33] Cuellar v. United States, 553 U.S. (2008), for example.

[34] KYC has become part of the mandatory requirements for financial institutions in demonstrating due diligence as part of Anti-Money Laundering AML/Countering Financing of Terrorism measures.

[35] For discussion, see Edna Kabala and Manenga Ndulo (2018) "Transfer Mispricing in Africa: Contextual Issues," *Southern*

Insofar as the profits would have been repatriated in any case, transfer pricing reduces the government's tax revenue but not the country's stock of capital. We nonetheless discuss it here because transfer pricing and capital flight share some of the same attributes.

Unlike misinvoicing for capital flight, the extent of which can be gauged by observing discrepancies in trading partner mirror-data, misinvoicing for transfer pricing occurs identically on both sides of the transaction. Overinvoiced imports (e.g., for intellectual property rights or the intra-firm provision of other services) have, as their counterpart, over-invoiced exports from the exporting country; and similarly, under-invoiced exports (e.g., of minerals) are matched by under-invoiced imports in the books of the importing country. This means that transfer pricing is not included in conventional misinvoicing adjustments used in capital flight estimation.

Transfer pricing for purposes of tax avoidance or tax evasion (the difference between these terms hinges on the legality of the practice) is a problem in both developed and developing countries. There is a widespread impression, however, that it is more pervasive in developing countries, and there is an emerging body of evidence that supports this belief.[36] A recent study of South Africa also reported the striking finding that the practice is highly concentrated amongst the largest multinational firms: the top 10 percent of foreign-owned firms accounted for 98 percent of the country's total tax losses caused by profit shifting.[37]

Despite multiple initiatives to curtail abusive transfer pricing, the problem persists. One reason is the growth of intra-firm trade worldwide. When a firm with worldwide operations puts a price on goods or services provided by one subsidiary to another, who is to second-guess its judgment as to the "right" price? Estimates of the magnitude of mispricing typically rely on information on counterfactual "arms-length" prices, when this is available, but mobilizing the results of such comparisons for legal and enforcement purposes is not a straightforward task even when the formal rules are clear and strict. In

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Africa Journal of Policy and Development, 4(1); and Tax Justice Network, "Transfer Pricing," at https://www.taxjustice.net/topics/corporate-tax/transfer-pricing/, accessed on 29 June 2019.

[36] See, for example, N. Johannesen, T. Tørsløv, and L. Wier, "Are less developed countries more exposed to multinational tax avoidance? Method and evidence from micro-data," Helsinki: WIDER, Working Paper 2016/10, revised version May 2017; and Petr Janský, Miroslav Palanský, "Estimating the scale of profit shifting and tax revenue losses related to foreign direct investment," Prague: Institute of Economic Studies.

[37] L. Wier and H. Reynolds, "Big and 'Unprofitable': How 10% of Multinational Firms Do 98% of Profit Shifting," Helsinki: WIDER, Working Paper 2018/111, September 2018.

reality, the rules often are neither, reflecting not only the weakness of governing institutions but also of the ability of powerful interests to shape the regulatory environments in which they operate. In seeking to play countries off against each other, multinational firms use their leverage to press not only for favorable rules but also for lower tax rates and for tax exemptions. Even in the face of urgent needs for revenue, governments often accede to their demands.

III. Capital Flight and Trade: Non-fuel Commodities

This section analyzes export and import procedures for non-fuel commodities, taking Nigeria as a case study. The following section does the same for fuel commodities. The goal is to illuminate the institutional foundations of capital flight, the way in which the structure of incentives influences the way in which the game is played. As this section demonstrates, the story is not just about innocuous statistical discrepancies, and the game is played across all sectors.

Export procedures

Primary commodities figure prominently in Africa's international trade. Table 1 presents resource intensity, defined as the ratio of primary exports to total exports, for African countries for which

Table 1: Resource Intensity in Selected African Economies

	Countries	Intensity Ratio
1	Algeria	0.98
2	Angola	0.96
3	Benin	0.83
4	Botswana	0.16
5	Burkina Faso	0.73
6	Burundi	0.76
7	Cameroon	0.91
8	Cape Verde	0.41
9	Central African Republic	0.57
10	Chad	0.95
11	Cote d'Ivoire	0.80
12	Democratic Republic of Congo	0.59

13	Egypt	0.58
14	Equatorial Guinea	0.96
15	Ethiopia	0.84
16	Gabon	0.95
17	Gambia	0.66
18	Ghana	0.69
19	Guinea	0.78
20	Guinea-Bissau	0.96
21	Kenya	0.69
22	Lesotho	0.08
23	Madagascar	0.53
24	Malawi	0.88
25	Mali	0.52
26	Mauritania	0.91
27	Mauritius	0.29
28	Morocco	0.36
29	Mozambique	0.88
30	Namibia	0.53
31	Niger	0.62
32	Nigeria	0.98
33	Rwanda	0.86
34	Senegal	0.66
35	Seychelles	0.88
36	Sierra Leone	0.40
37	South Africa	0.45
38	Sudan	0.86
39	Swaziland	0.41
40	Tanzania	0.60
41	The Republic of Congo	0.92
42	Togo	0.63
43	Tunisia	0.23
44	Uganda	0.79
45	Zambia	0.85
46	Zimbabwe	0.69

Notes: "Resource intensity is the ratio of primary exports to total exports and indicates the importance of this category of export for trade and growth, including foreign currency revenue. A high resource-intensity ratio is problematic because it indicates fragility regarding ability to finance development expenditure that invariably requires availability of hard currencies. For Tanzania, the period covered for the resource intensity data is from 1999 to 2013 instead of 1995 to 2013 as is the case for the rest of the countries. So, 5 years of data is missing for Tanzania. The mean of the sample = 0.69, the variance = 0.06, and min-max values = (0.08,0.98).

Source: UNCTAD data reported by Ayogu, Melvin D. and Kingsley Onyeka "Are you being served: Governance and Deprivation" *CWP # 181011 - CPPA Studies on Inequality, Human Development and Economic Transformation.* http://cpparesearch.org/nu-en-pl/#

the pertinent data are available. In the majority of the 46 countries profiled, the ratio stands at more 50 percent. Crops are the most widespread of the tradeable primary commodities. They include traditional export crops such as cocoa, coffee, sugar and cotton; cereals such as maize, wheat, sorghum, barely rye, oats, millet, and rice; oil crops such as palm oil, soybean, sunflower, rape seed, groundnut, sesame, and coconut; roots and tubers such as cassava, cocoyam, and yam; fruits and vegetables; and tobacco. Important solid minerals found in the continent include gold, silver, platinum, tanzanite, aluminum, palladium, diamond, manganese, cobalt, phosphate, bauxite, tin, tantalum, and tungsten. Although less well-known than its petroleum resources, Nigeria produces a wide variety of solid minerals, most of them are found in the Northern, Middle Belt and Western parts of Nigeria with concentration in Plateau State and Western States.[38]

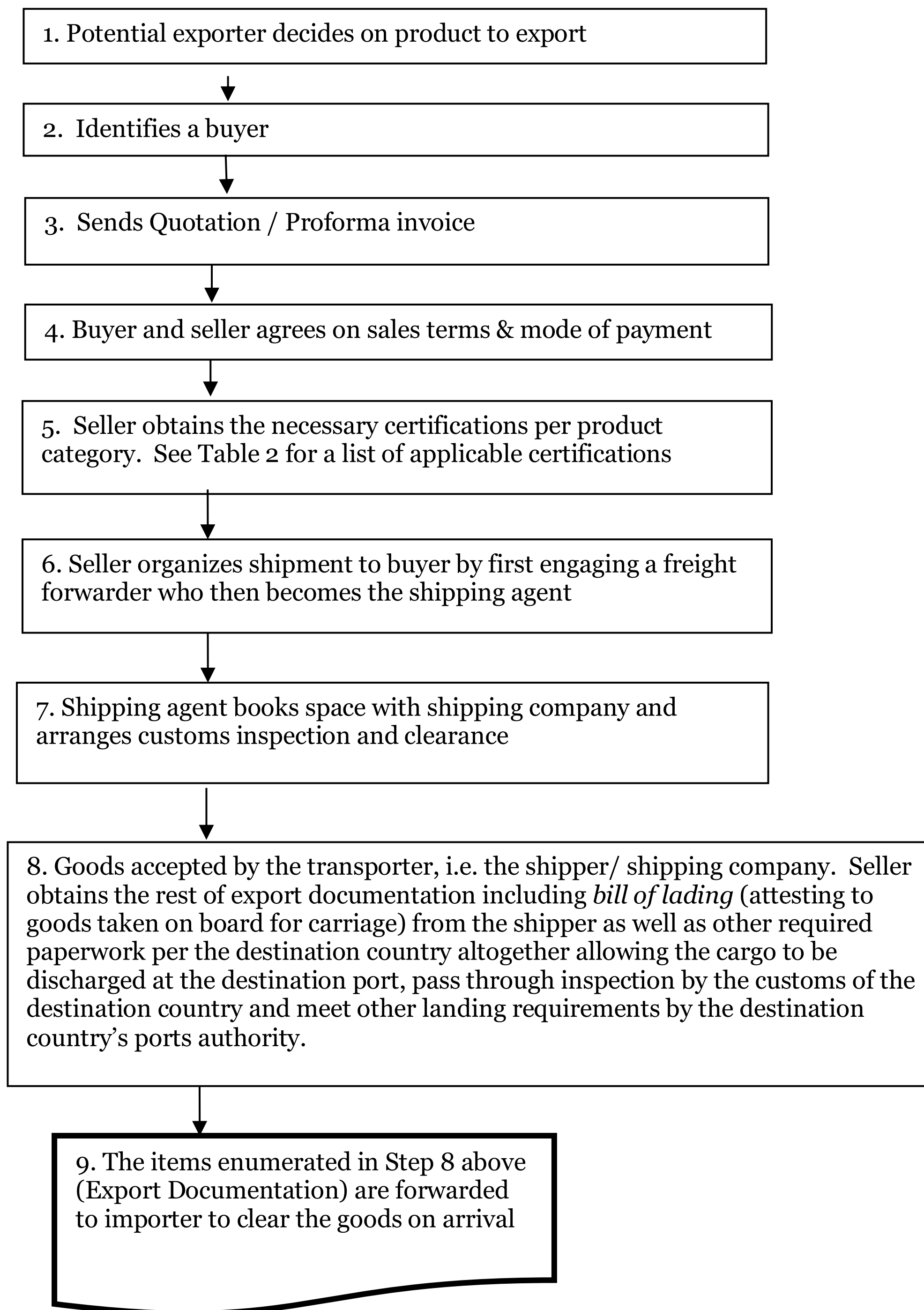
The formal rules for exporting non-fuel commodities from Nigeria are summarized in the flow charts shown in Figure 2A. The first step for a prospective exporter is to register with the Corporate Affairs Commission and subsequently with the Nigerian Export Promotion Council (NEPC). Provided the exporter meets the registration requirements, NEPC issues a certificate that the entity is now a recognized exporter in Nigeria.

Seventeen additional export certificates are on the menu at step 5, depending on the product and the country of destination (see Table 2). Free ports and trading hubs are particularly significant for items 3 to 5, namely, certificates for cocoa levy, tariff concession for North-South trade, and export facilitation schemes for intra-regional trade. Securing the trade advantages promised in these schemes is based on declarations regarding origins and destinations of the commodities. These requirements can be readily gamed using the opportunities provided by trading hubs, as discussed above.

The export procedure for non-fuel minerals, as recounted in an interview with an operator experienced in both solid minerals and agricultural commodities, yields a parallel but different narrative.[39] Informal rules and norms complement the formal rules laid out above, shaping the underlying incentive structure. The exporter's goal is to retain the maximum possible proceeds from the export. In principle, a duly

[38] For details, see: Nigerian government, "Nigeria Natural Resources". Available at http://www.nigeria.gov.ng/index.php/2016-04-06-08-38-30/nigeria-natural-resources. Accessed on 1 August 2019
[39] This account is based on an interview conducted in Lagos Nigeria in 2018.

Figure 2A: Procedure for General Merchandise (excluding Oil and Gas) Export in Nigeria



Source: Narration based on the flow chart in Madu, O (2015), "Trader Journey," mimeo, Multimix Academy, Lagos, Nigeria.
Notes: The flow chart assumes that the exporter is licensed, meaning that all necessary requirements for issuing export license have been met and that the enterprise has a functional bank account.

Table 2: Types of Export Certificates in Nigeria's Export Regime

	Title of Document	Use(s) of The Document	Where Obtainable
1.	Exporters Registration Certificate	For Identification of Nigerian Exporter	Nigerian Export Promotion Council (NEPC)
2.	Sanitary and Phytosanitary Certificate	Conditions for both exporting and importing countries to ensure safety in the handling of Agricultural product and natural resources free from diseases	Nigeria Agricultural Quarantine Services (NAQS)
3.	ICCO-1 Certificate	It is a combined certificate of origin and declaration of value for cocoa levy	Federal Ministry of Industry, Trade and Investment, (FMITI) Produce Inspection Unit
4	GSP Form	For tariff concession for all countries involved in North-South trade	NACCIMA, NCS
5.	ECOWAS TLS Certificate	For goods trade under the ECOWAS Trade Liberalization Scheme	NEPC, Ministry of foreign affairs and ECOWAS Secretariat
6.	Form J	Clearance letter for the export of solid minerals	Federal ministry of solid minerals development and Nigerian mining corporation
7.	Certificate of clearance from veterinary Health Services	Certificate of clearance from Veterinary Health Services	Department of Veterinary health services, Federal Ministry of agriculture
8.	Certificate of clearance from national commission for museums and monuments	For exports of handicrafts and artefacts	National Commission for Museums and Monuments
9.	Clearance from department of forestry	For exports of classified endangered wild life species and wood products. Furniture and furniture components	Department of forestry, federal ministry of agriculture
10.	NXP Form	For commercial exports originating from Nigeria	CBN and Commercial Banks
11.	Non-commercial Exports (NCX) Form	For non-commercial exports	CBN and Commercial Banks

12.	NIMASA Form C series	For allocation of cargoes to shipping lines. It serves as cargo tracer and loading authorization to allotters.	NIMASA and commercial Banks
13.	Single Goods Declaration (SGD) Form C2C10	Gives details of consignments	NCS
14.	Certificate of quality for food, drugs and cosmetics	Certifies the quality of foods, drugs and cosmetics meant for exporters	NAFDAC
15.	Certificate of quality	For manufacturers only	SON
16.	Certificate of analysis and quality	To certify the quality of a product in question	Issued by manufacturers, processors or miners
17.	Certificate of quality and fumigation	To certify quality of raw agricultural commodities	Federal produce inspection service
18	Bill of lading and airway/roadway bill	Evidence of carriage of goods	Shipping company/transporter

Source: Nigerian Export Promotion Council, www.nepc.gov.ng.

Key: CBN=Central Bank of Nigeria, ECOWAS=Economic Community of West African States, NACCIMA=National Association of Chambers of Commerce Industry Mines and Agriculture, NCS=Nigeria Customs Service, NAFDAC=National Agency for Food and Drugs Administration and Control, NEPC=Nigeria Export Promotion Council, NIMASA=Nigerian Maritime Administration and Safety Agency, SON=Standard Organization of Nigeria.

registered Nigerian exporter is required by law to surrender all export proceeds to his or her bank for conversion to domestic currency at the official exchange rate, which is invariably lower than the market rate.[40] This policy is viewed by exporters as a tax. Like other taxes, it is considered unduly burdensome in light of the poor delivery of public services and the perception of a high incidence of kleptocracy.

The rules also allow the exporter to deposit revenues into a foreign currency export revenue account (called NXP account), from which the exporter can draw foreign currencies for specific approved purposes. Alternatively, having converted the export-revenue to domestic currency at the official exchange rate, the exporter is supposed to be able to purchase foreign currency for approved purposes at the official rate, which is less expensive than the market rate. In practice, however, the experience of attempting to follow this procedure often proves frustrating, forcing many exporters to source funds

[40] The parallel market premium has averaged about 20 percent which also is the current markup over the official rate.

outside the more attractive government rates. The process for getting approval to purchase foreign currency at the preferred rate can be dilatory, and it is open to bribery and corruption.

The conduct of the exporters could be considered rational responses to the numerous challenges of doing business in this environment. Figure 2B is an augmented version of Figure 2A, with a focus on the money trail. In Step 1 the exporter selects a mode of payment that maximizes the likelihood of securing the expected export proceeds. This would be a mode that is sufficiently robust to address known and unforeseen contingencies.

Figure 2C depicts a process that games the steps shown in Figure 2B, so as to circumvent the constraints imposed by the formal rules. Because formal export channels are often cumbersome and slow, an exporter of merchandise with a short shelf life will preselect the informal channel, and factor into the negotiated export price the premium from using the informal channel. Having decided to go the illicit route, an exporter's further consideration would be the destination of the proceeds, which also determines the mode of payment. Thus in making the first decision in the chain depicted in Figure 2B, the exporter takes a panoramic view of the entire chain.

The routine described in Figure 2C is not hypothetical. In fact, the governments of some of the federated States of Nigeria and other interested parties have openly accused the Federal Government of Nigeria of "lacking the political will to implement mining [regulations] because of vested interests."[41] An estimated sum of one billion dollars is claimed to have been lost over three years by the Nigerian government due to gold smuggling, one of the many minerals conveniently falling under the government's blind-spot.[42]

The complexity of Nigeria's export protocols pale by comparison to the process for exporting goods from South Africa, and not to some faraway land such as New Zealand but to a neighboring African country which also belongs to the same customs union, the South African Development Community (SADC). An infographic account of the experience of a South African exporter, as reported by the Chief Executive of the Consumer Council of South Africa, is depicted in its entirety in the Appendix.

[41] "Nigeria loses N353bn to illegal gold mining in three years, IYC, Bayelsa kick", *Punch,* 17 April 2019. Available at https://punchng.com/nigeria-loses-n353bn-to-illegal-gold-mining-in-three-years-iyc-bayelsa-kick/, accessed on 1 August 2019.

[42] *Ibidem.*

Figure 2B: Export Procedure for General Merchandise (excluding Oil and Gas) Export in Nigeria

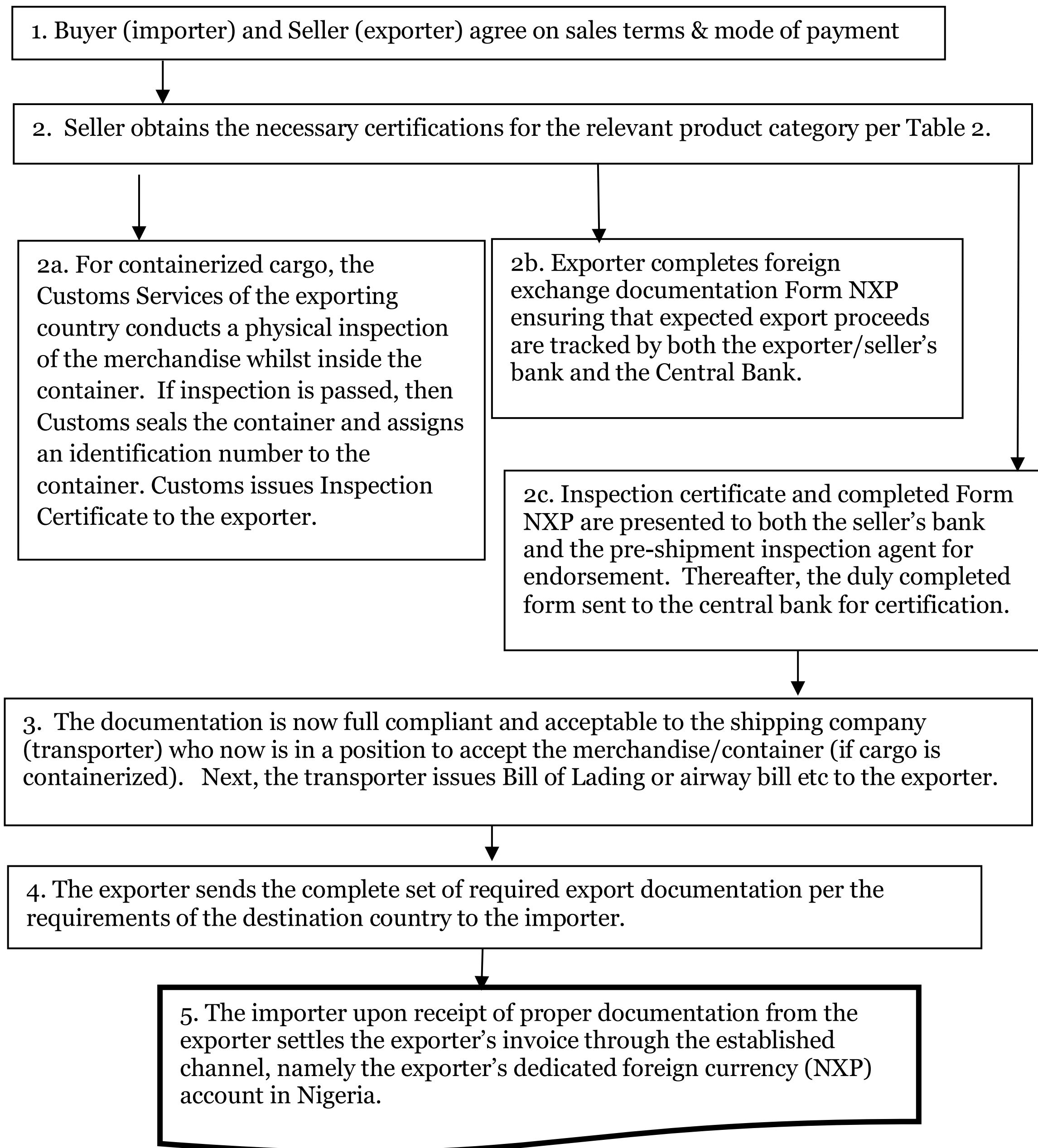


Figure 2C: Exporter Response to Institutions (Incentive Structure) Governing Exports of General Merchandise (excluding Oil and Gas) in Nigeria

The Challenge

For a majority of the merchandise under consideration, time-to-market is so much faster when transacting through the informal channels than through the formal channel. The time differential is said to exceed one month on average. For seasonal commodities, such a delay from transacting through formal channels imply potential revenue losses which, in conjunction with the foreign exchange loss on conversion of export revenue, reduces expected profit. The informal channel takes between 1-3 days to conclude, at least for charcoal and solid minerals. Formal export channels entail inspection and clearances from relevant agencies and ministries, often involving significant delays, leading to desperation, bribery and corruption.

Exporter Recursive Solution to the Export Challenges

1. Rank probable safe havens for the expected export proceeds. Options include hiding some of the funds in the Republic of Benin, Togo, Ghana, Kenya, USA, UK and Switzerland. Current UK rules and regulation have been lately viewed as tough and pro Nigeria's anti-corruption measures whereas Switzerland is perceived to have warmed up to mutual legal assistance with Nigeria thus also making it a less desirable jurisdiction for money laundering.

2. Conditional on options in Step 2, agree on terms of the sale and mode of transaction including preferred method of settlement: Misinvoicing, barter, or false declaration of merchandise? In a false declaration, for example, lead ore is declared whereas importer pays for platinum, the commodity that is actually shipped and received.

3. Follow the formal channel.

4. If so, then engage special freight forwarders. These special forwarding agents have cultivated relationships with customs and shipping companies that enable them to fast-track the process to Bill of Lading, bypassing Form NXP. Expedited services attract "non-documentation" premium.

5A. Fast-tracking the process in Step 5 may involve circumventing export inspection by bribing the authorities. This an especially attractive option when transporting low bulk, high value items such as gemstones. In such cases, shipments through courier companies are equally appealing. Some couriers may transport without a full suite of documentation. The core of the incentive—the value proposition—is to secure cross border shipment without complying with the Form NXP protocol. To the exporter, this means securing efficient commodity movement without the money trail.

5B. As an alternative to 6A, skip shipment entirely and instead transport the gemstones on board an airplane as a cabin baggage, booked in first class or business class. Arrive overseas destination and sell merchandise in any of the open-markets such as Hatton Garden in London, UK; Antwerp, Belgium; Munich, Germany; Bangkok, Thailand; and Colombo, Sri Lanka.

South Africa's elaborate export protocol is presumably designed to safeguard expected export revenue of a country that cares very much about its fiscal circumstances, avoiding any potential leakages. The items of apparently keen interest to the authorities include a common brand of rice (Tastic), tea bags, mayonnaise, sugar, laundry detergent, dish washing liquid, deodorant, milk, canned vegetables, maize meals, frozen fish, chicken, and fruit. A typical container load of an assortment of these items requires 83 sets of documentation in 634 pages carrying 56 signatures of customs officials and 84 custom stamps. In the fiscal year ended June 2016, for example, 1262 shipments to Angola involved 64,362 sets of documents containing 758,462 pages. Don't mess with South Africa's export revenue is the clear message.

If this is so, then the question that must be asked is why would a country with such rigorous procedures for the export of tea bags, tomato ketchup, mayonnaise, and detergents treat its gold exports "as a country?" Besides its absurdity, why is there, in effect, a lower degree of diligence regarding records of exports of this particular commodity? Why does this not raise persistent questions within the society? Even if such treatment were thought to be rooted in the country's apartheid past, when evasion of trade sanctions could have been part of the motive, why have these "legacy rules" persisted long past 1994, when the new South Africa was born? The "bubble," as the state calls it, where users of trade data "will not be able to determine where the exports are going to or the imports are coming from," is comprised of "95% gold."[43] This unconventional administrative procedure raises more questions than it provides explanations of South Africa's recording protocols for international transactions.

Import procedures

In comparison with Nigeria's export requirements, its import protocol appears to be even more cumbersome. The process is described in detail in Tables 3 and 4. There are three salient points to note. The first is to recall that in the export protocol described earlier, an important consideration for exporters is time-to-market, which can be subject to significant dilatory tactics in the formal channel, thus creating opportunities for alternative options to be attractive. Similarly, the threat of demurrage charges, levied

[43] SARS, "Explanations and notes". Available at http://www.sars.gov.za/ClientSegments/Customs-Excise/Trade-Statistics/Pages/Explanations-and-Notes.aspx, accessed 1 August 2019.

by shipping firms when unloading of the cargo is delayed, given a cumbersome import process vulnerable to dilatory tactics, also creates opportunities for informal side payments, an example of what economists call "rent seeking." As the American legal scholar and behavioural economist Cass Sunstein has observed in a different context, "administrative burdens are an emphatically political choice."[44]

One way of boosting profits, as well as to recoup such informal "costs of doing/expediting business," is to reduce the duty payable by filing false declarations of the goods or their value (misinvoicing) and then bargaining over the distribution of the differential amongst the players.

The second point to note is the requirement for importers to apply for approval from the Central Bank for the purchase of foreign currency to settle the invoice. This leads to the practice of importer paying for "sawdust" – ghost (or overvalued) imports – as a means of relocating scarce hard currency overseas under false pretenses. This currency is obtained from the Central Bank at the official rate, which is more favorable than the market rate. Indeed, merely selling the currency thus obtained on the market would yield a tidy profit.

The third point is that there are two nodes in the customs clearance protocol at which a false declaration can, in principle, be detected. The first is at Step 15 in Table 3, where the risk channels are assigned and implemented. The other is at Step 26 of the sub-process described in Table 4 when the container is exiting the gate with the merchandise. Random inspection can detect a false declaration. A false declaration leading to a higher duty will trigger a Debit Note (DN) requiring the importer to pay additional charges. For our purposes, we are interested in whether such an adjustment will lead to a revision of the data captured at the Data Transmitting Interface (DTI) at Step 11 in Table 3. Our inquiries on this point elicited the information that ordinarily the DN is appended to the original set of import documentation, but whether the data revision is made is an open question.

[44] Cass R. Sunstein (2019) "Wading Through the Sludge," *New York Review of Books,* 4 April. Sunstein was referring to the U.S., where burdensome administrative procedures have been used, for example, to restrict voter registration. In other settings, the motives may have more to do with opportunities for pecuniary gain.

Table 3: Description of General Merchandise Import Process – Nigeria

1. Importer identifies a supplier/exporter and agrees to deal.
2. Exporter sends pro forma invoice to importer. Importer arranges insurance accordingly.
3. Importer arranges payment: obtaining foreign exchange domestically; prepayment using an account overseas or enters into an international trade financing arrangement.
4. Importer opens a Form M on the Nigerian Trade Platform (Single Window) system. Form M and other applicable documentation are submitted to importer's bank.[45]
5. Bank reviews documentation for compliance. If validated then, submits the Form M to customs for approval.
6. Upon approval, importer authorizes the issuance of Letter of Credit if applicable and informs exporter to ship goods.
7. Exporter sends shipping document through her bank/ importer's correspondent bank for onward transmission to importer bank.
8. Bank forwards final shipping documents to customs for Pre-Arrival Assessment Report (PAAR).
9. Importer collects PAAR from bank and passes it to her clearing agent to work it through the clearing process for the release of the cargo (see Table 3 for details of the daunting clearing sub process).
10. Agent receives PAAR and confirms steamer or airline/transporter arrival and position of cargo.
11. Agent lodges Single Good Declaration (SGD) at the Data Transmitting Interface (DTI) café which generates assessment notice indicating import duty to be paid.
12. Agent pays duty at a bank as indicated on the assessment notice and gets payment receipt from bank.
13. Agent returns to DTI café and inputs payment details which generates risk channel, that is, level of Government intervention.
14. Depending on the risk channel, the clearing agent follows the process for the risk channel generated for the transaction in question.
15. There are 5 risk channels namely Blue, Green, Yellow, Light Red and Deep Red.
16. Blue Channel is known as fast track for big manufacturers. They receive cargo at ship side and immediately relocate cargo to their warehouse. The company notifies the Post Clearance Unit of the Customs for inspection formalities which will be done at company/warehouse premises. Cargos are not touched until arrival of the Unit.
17. The green channel is for importers who have maintained a clean profile over the years. This channel allows this class of importers to take delivery of their consignments from the terminal after performing the shipping and terminal operator formalities. This may not always be the case as some transactions channeled to green are rerouted to Deep red.
18. The yellow channel indicates that a documentary check is required at the Customs Processing Center (CPC). The importer goes to the Query and Amendment seat at the C.P.C to confirm the details of the transaction as earlier declared and thereafter takes delivery of cargo once shipping and terminal formalities are completed.
19. The Light Red indicates that the shipment would go through a scanning process to confirm the nature of what is concealed as against what is declared.
20. The Deep red channel indicates that a full physical examination would be done on the consignment.
21. Customs broker gets Exit Notice indicating formal release of cargo after due process.
22. The Exit Notice is required for Shipping line and terminal operator's release.
23. Customs broker gets a Debit Note which indicates the shipping charges and pays for charges at a bank.
24. The payment receipt, the Exit Notice and other documents in the SGD is used to obtain Shipping Release and Delivery Order. These documents are then taken to the terminal operator's office for settlement of terminal charges. Once payment is made and all documents attached, the terminal operator issues a Terminal Delivery Order (T.D.O) that is then used to move consignment out of the terminal and port.

Notes: Author's compilation and verification of documents based on Madu, O (2015), "Trader Journey," mimeo, Multimix Academy, Lagos, Nigeria and information from http://nigerianports.gov.ng/import-export-guidelines-3/

[45] Form M is the template for an application for exchange control approval to purchase foreign currency from an authorized bank at the official rate much lower than the market rate that trades on the average at 20 percent premium.

Table 4: Description of General Merchandise Import Clearing Sub-Process (in Step 9 of Table 3)– Nigeria

1. The Declarant prepares the customs entry called Single Good Declaration (SGD). The SGD is a form in 8 copies that will be dispatched to various parties during the clearance process. The information on the SGD is captured at the Data Transmitting Interface (DTI) café. The declarant must have obtained a Risk Assessment Report (RAR) from Cotecana before preparing the Customs entry. The declarant also assesses his declaration. The assessment, based on the documentation of the import transaction, indicates the amount to be paid as duty by the declarant. The declarant prints assessment notice at DTI which carries all duties and taxes relating to customs release.
2. The declarant goes to the bank with the assessment notice and makes payment of the assessed value. Bank issues declarant Payment Acknowledgement sheet. The payment is electronically transmitted to the Customs system. The declarant then goes to CPC for consignment release.
3. NCS confirms payment at CPC and releases consignment by printing Exit note which is given to declarant.
4. Declarant takes original copy of B/L to shipping line for a copy of Debit Note or invoice which indicates the amount to be paid for shipping release after collection, the declarant goes to the bank and makes payment as reflected on Debit Note.
5. The declarant then takes the payment teller from bank and other documents listed above to the shipping line for a receipt and Delivery Order respectively.
6. Declarant takes Delivery Order (DO), Bill of Lading and receipt of invoice to the office of the terminal operator for Payment Invoice which indicates how much is to be paid as Terminal charges.
7. The declarant goes to the bank for payment of terminal charges.
8. Declarant then takes bank teller along with other documents required for terminal release to terminal operator's office for collection of Terminal Delivery Order (T.D.O). Declarant gives T.D.O, letter of Authority and Identification card to driver to enter the port for loading of cargo.
9. Driver comes into the terminal to load and then drops the T.D.O at the terminal Operators office at the exit gate and collects Equipment Interchange Report (EIR). Steps 1 to 5 are similar for the Green channel.
10. Declarant goes to Terminal operators' office to book for physical examination at terminal.
11. Terminal Operator drops container at terminal for physical examination
12. Declarant goes for allocation of entry, collects examination form and confirms NCS officer assigned to undertake physical examination at terminal.
13. Assigned NCS officer for physical examination endorses examination form.
14. Declarant cuts container seal and invites other government agencies mandated to observe and confirm examination.
15. Examination agencies, in the presence of declarant, physically examine containers.
16. Declarant gets examination report from resident NCS officer
17. Declarant takes examination report to Chief Examiner for endorsement
18. Declarant takes examination report to Valuation Unit for endorsement.
19. Declarant takes examination report to Task Force for endorsement. Task Force at Terminal may refer declarant to Task Force main office for clarification before commencement of procedure.
20. Declarant takes examination report to Officer-in-Charge (OC Terminal) for endorsement and release.
21. Declarant goes to NCS Resident officer for electronic transfer of release to Terminal Operator
22. Declarant goes to terminal operator's office for Exit Note and then applies for T.D.O.
23. Declarant collects T.D.O, attaches all other documents and takes them to Enforcement Unit at Terminal for endorsement.
24. Declarant takes documents to the CIU office at Terminal for endorsement. CIU at Terminal may refer declarant to CPC for clarification before commencement of procedure.
25. Declarant takes all documents to Gate Control Unit at the gate for endorsement and collects Exit to leave the port.
26. If container is examined and found to contain under declared goods, Debit Note is raised by NCS for payment. Declarant continues with process after payment. However, if container is found to contain prohibited items, documents are held by NCS and transferred to Enforcement Unit for action.

Notes: The original source is O. Madu (2015), "Trader Journey," mimeo, Multimix Academy, Lagos, Nigeria, with modifications and updates by the author.

The foregoing descriptions of the trade protocols in Nigeria and South Africa (the two largest economies in Africa) are meant to convey the nature of the environment governing the transactions summarized by official data on exports and imports. Additionally, it is meant to raise the level of appreciation of why it is challenging to secure the compliance of sovereign nations with rules of data reporting designed to harmonize the processes behind the data. If achieving consistency across counterparties to the same transaction is difficult, the inferences and conclusions from official data rest on fragile foundations. This situation is presumably of serious concern to scholars and policymakers alike.

There are several takeaways from this fuzzy data terrain. First, a great deal more effort should be directed at clarifying, validating, and harmonizing international trade data. Second, some initiatives to improve trade data reporting are finally beginning to happen in this regard, as noted above.[46] Third, equally helpful would be the adoption of a more open-minded view regarding some of the more embarrassing perspectives on trade data discrepancies. Such a disposition may be constructive, leading to useful enhancements of data quality, particularly if suspected leaks in the current system are followed up, investigated, and found to exist. But progress along these lines cannot occur in an atmosphere of mutual distrust, automatic denials, self-serving arguments, and attempts to discredit unwelcome views.

Researchers working on Africa's development challenges conduct data-based empirical analysis to make inferences, including observations that African states tend to be fragile, dysfunctional, corrupt, and characterized by low growth, high poverty, and high income inequality.[47] Yet few of those analyses ponder the conundrum in using the available data to assess outcomes without worrying about the quality of the data emerging from such arguably dysfunctional environments. It is as if, by some divine exception, data issues were immune from the influence of the constraining factors and development failures that are the subject of the analyses. How can all else fail except the reliability of the data used to

[46] The Automated System for Customs Data (ASYCUDA), developed by UNCTAD, is a specific example of efforts to improve the documentary procedures—process and control—in international trade. ASYCUDA is an integrated customs management system for international trade and transport operations in a modern automated environment, designed to improve security by streamlining procedures of cargo control, transit of goods and clearance of goods, and to help the fight against corruption by enhancing the transparency of transactions. See https://unctad.org/en/Pages/DTL/TTL/ASYCUDA-Programme.aspx, accessed on 3 October 2019.

[47] For perspectives on the Afro-pessimism literature, see John Sender (1999) "Africa's Economic performance: Limitations of Current Consensus," *Journal of Economic Perspectives* 13(3): 89-114.

determine the failure? The implication is that serious, concerted efforts to improve data quality should be a central item on development agendas.

IV. Capital Flight and Trade: Fuels

Using UNCTAD data, primary commodities account for 98 percent of Nigeria's export revenue (see Table 1). Oil and gas dominate the country's exports.[48] Not surprisingly, the Federal Government of Nigeria has devoted much attention to the regulation and monitoring of the trade in fuel.[49] It is of great interest, therefore, to ask how a barrel of Nigeria's oil moves from the point of extraction, the well head, to the point of sale (POS) where property rights are exchanged.

The paper trail

Three aspects of the upstream value chain – substance, displacement, and custody –are crucial for understanding the phenomena of pilfering, smuggling, and false declarations.

Substance refers to gradations in the quality of the crude oil that are reflected in their market price. These variations in quality are measured as API (American Petroleum Institute) gravity differentials. The two major categories are light and heavy crudes. Light crudes are preferred and command a higher price. Heavy crude oil contains more impurities which must be removed to produce the substance for which value will be exchanged. Primary processing at the wellhead separates oil from gas and water. Additional segregation can occur during bulk transportation in vessels prior to the cargo's arrival at the point of sale. The extent of segregation and evaporation depends on the duration of the carriage. Furthermore, temperature variations can induce natural separation of water

[48] In 2016, oil and gas accounted for 92.3 percent of export revenue. Of the rest, agricultural commodities account for about 3 percent comprised mainly of cocoa beans, sesame seeds, and cashew nuts. See Central Bank of Nigeria, Annual Report 2017, available online https://www.cbn.gov.ng/Out/2018/RSD/CBN%202017%20ANNUAL%20REPORT_WEB.pdf, accessed on 3 October 2019.

[49] In contrast, the non-fuel minerals have been left unattended by the Federal Government of Nigeria. This imbalance in attention on Nigeria's natural resource types has drawn pointed criticism from Nigeria's oil producing States, who accuse the Government of sharing the wealth from the south, where the oil and gas emanate, and leaving the revenue from non-fuel minerals largely mined in the north of the country to be monopolized by the producing States.

and oil. For these reasons, readings taken at flow stations after primary processing can vary. The designation of oil as "export quality" instills some level of certainty in the determination of its quantity. Once crude oil is certified export quality, it is locked in for revenue accounting such that any further variation claims have to be established convincingly.

Displacement describes the flow path from wellhead to flow station to export terminal. Flowlines connect individual wells to the flow stations (where gas and water separation occurs), while pipelines connect the flow stations to the terminals. Export terminals are designated points of sale. "Bunkering" (the illegal pilfering of crude oil) can happen along any segment of the flow path from the wellhead to export terminal. The operators usually own the flowlines from wellhead to the flow stations. Some of the pipelines are owned and operated by the Nigerian Pipeline Development Corporation (NPDC), a subsidiary of the Nigerian National Oil Corporation (NNPC), while others are owned and operated by independent oil companies (IOCs). Following a wave of divestment of onshore assets by IOCs, ownership of some of the major pipelines was transferred to joint ventures between NPDC and indigenous companies that operate the pipelines.

Custody refers to chain-of-custody control protocols, the verification mechanisms attendant to the barrel of crude as it transits from wellhead to flow station to pipeline to export terminal or final point of sale. Where the standard fiscal meter is not available at the export terminal, the out-turn, where the crude is transferred to the purchaser, becomes the POS at which contractual export volumes are determined. Some offshore and deep-water production is stored on floating storage facilities and these are also designated as terminals for export.

Until the year 2000, the integrity of Nigeria's displacement and custody processes could not be guaranteed. "Monitoring" of activities basically was a matter of accepting production numbers from the field rather than using fiscal meters to capture data on production and export-bound volumes at transfer points. Now meters installed at wellheads record the quantities transferred to flow stations for primary processing. The Department of Petroleum Resources (DPR) within the Ministry of Petroleum Resources is the industry regulator accountable for all matters pertaining to crude quality, chain of custody and verification mechanisms. It is a DPR regulation that it be present at each out-turn.

Fiscal meters are installed at flow stations to record quantities after primary processing, prior to injection into the pipeline for transfer to the export storage terminal, pending sale. Evaporation and further separation while in transit means that for overseas sales, the volume may have changed materially from the volume at the export terminal. Revised volumes at point of sale would have to be verified on behalf of all parties. The buyer usually gives the final volume when transferring the crude oil to the refineries. In some cases, DPR representatives are present to witness the verification of quantities.

Production from some offshore facilities flows to export terminals via pipelines, but in other cases the oil goes instead to floating storage facilities. In deep-water production facilities the wellhead lies at the seabed and flowlines and risers transport the crude oil to a floating production, storage and offtake platform (FPSO).[50] On the platform, water is removed, treated and discharged—primary processing—and crude oil is stored. The fiscal meter on the FPSO records the quantities stored in tanks on the platform. Lockdown valves at each discharge point have tamper-proof seals and are under the watch of four independent overseers, Customs, the Department of Petroleum Resources, the operator, and an independent auditor. The keys to the locks are in the custody of the DPR and Customs, and they must be engaged simultaneously to release and open the valves.

The FPSO is a designated export facility. As such, it has defined exclusion perimeters under the protection of the state. The maritime exclusion zone is a five-kilometer radius protected by the Nigerian Navy and monitored from the FPSO. Daily production is reported and recorded. When a required export threshold is attained, application is then made to DPR for an offtake permit. On that basis, DPR assigns an allowable export volume with concurrent notification of the assignment to the Customs as well as to a subsidiary of NNPC, the Crude Oil Marketing Department (COMD). It is the duty of COMD to obtain samples of all the crude oil produced to determine the blend as well as the reference sales price. DPR, the regulator, is present to conduct verification during transfer from the FPSO to the offtake tanker.

The oil company (vendor) pre-registers the pending transaction as well as the identity of the transporter. When the offtake vessel is 30 kilometers away from the terminal, the vendor is notified who in turn notifies the DPR and the ports authorities to grant entry clearance to the offtake vessel. Additional

[50] Our account here is based on an interview on July 1, 2018 with Mr. Peter Oriaifo, CEO Erin Energy in Lagos, Nigeria, with editorial comments from Segun Omidele and Chris Arima of Neconde Energy.

oversight by the Nigerian Maritime and Safety Administration Agency (NIMASA) monitors all maritime traffic regarding vessel specifications, capacity and destination as well as compliance with safety regulations in Nigerian waters.

Leakages and non-transparency

The foregoing description of the chain of custody for tracking crude oil from extraction to POS confirms that the state can track the commodity with a view to verifying production and sales volumes. Whether it does so accurately is another matter. So-called "leakages" – unauthorized diversions of oil into private hands – occur from the wellhead to the terminal, with an assortment of players involved in a racket known as illegal bunkering. There are no reliable data on the scale of the phenomenon, but observers often place it at 10-20 percent of oil production, with some operators claiming even higher percentages.

Concerns have been expressed repeatedly about the lack of transparency and accountability in oil deals and the lack of credible repercussions for transgressions. These concerns extend beyond Nigeria and have found a collective voice in the Extractive Industries Transparency Initiative and the *Publish What you Pay* campaign.[51] Credible commitments to authentic verification schemes are key to restoring faith in future numbers.

The revenue realized from crude oil sales is a function of transaction prices as well as quantities sold. Opacity in either of the two dimensions renders the revenue figures dubious. Even if the quantities of oil sold were known with reasonable certainty, they tell little about total revenue because this magnitude depends on what the NNPC decides to disclose to whom and when and on the validity of that information.

Officials with the Central Bank of Nigeria say that data on crude oil revenue reported in the country's Balance of Payments accounts are based on unsubstantiated figures from the NNPC. The Central Bank accepts the data on an as-is basis, having no powers or instrumentality with which it can independently

[51] On the Extractive Industries Transparency Initiative, see https://eiti.org/, accessed on 1 August 2019. On the Publish What You Pay campaign, see https://www.pwyp.org/, accessed on August 1 2019

audit NNPC submissions.[52] But it should also be noted that the Department of Petroleum Resources is supposed to possess accurate data on export volumes and earned revenue. In theory, therefore, NNPC's data should be verifiable by reconciliation with that held by DPR.[53]

Numerous assessments of the NNPC have indicated that it may be the most opaque governmental institution in Nigeria. A 2014 study conducted by the Nigerian Natural Resource Charter and the Centre for Public Policy Alternatives characterized the NNPC as having "scarce or inadequate information, insufficient audits, and poor financial reporting standards," and concluded that "complexity and opacity in public revenue procedures have undermined oversight efforts by civil society actors."[54]

In 2014, the former Governor of the Central Bank of Nigeria, Sanusi Lamido Sanusi, declared that "NNPC has in violation of the law and constitution been diverting money from the Federation Account [the central government treasury], and involving itself in activities that warrant full investigation for more serious violations of the law."[55] A subsequent forensic audit report by the international accounting firm PricewaterhouseCoopers (PwC) found an $18.5 billion gap between sales and cash remitted to the government in a 19-month period from January 2012 to July 2013, of which, according to Sanusi, about $12.5 billion appears to have been "diverted."[56]

In her book, *Fighting Corruption is Dangerous*, former Finance Minister Ngozi Okonjo-Iweala writes that "the story of Nigeria's oil and gas sector is ugly":

[52] Transcript of interview on July 9, 2018 with officials in the Statistics Department of the Central Bank of Nigeria.

[53] For data on natural gas, the unaudited information reported in the BoP is obtained from the Nigerian Liquified Natural Gas Limited. For other merchandise exports, the BoP data are obtained from customs services and licensed pre-shipment inspection agencies who by law are obligated to submit their data directly to the Central Bank.

[54] Natural Resource Charter and Center for Public Policy Alternatives, *Summary of the 2014 Benchmarking Report: Assessing the governance of Nigeria's petroleum wealth*. Lagos: Center for Public Policy Alternatives, 2014. Online at http://cpparesearch.org/nu-en-pl/wp-content/uploads/2015/01/NNRC-Summary-Briefing_December-2014.pdf, accessed on 22 July 2019.

[55] Sanusi Lambido Sanusi, "How NNPC Illegally Diverted $20 Billion from the Federation Account," *Sahara Reporters,* 5 February 2014. Online at http://saharareporters.com/2014/02/05/how-nnpc-illegally-diverted-20-billion-federation-account-cbn-governor-sanusi, accessed on 22 July 2019.

[56] Sanusi Lambido Sanusi, "Unanswered questions on Nigeria's missing oil revenue billions," *The Financial Times,* 13 May 2015. Online at https://www.ft.com/content/e337c7a4-f4a2-11e4-8a42-00144feab7de, accessed on 22 July 2019.

> The impact of the sector has fallen far short of expectations because of inappropriate policies, inefficient and nontransparent institutions, corruption, capture by leaders, and rent-seeking internal and external elites. This makes the sector a minefield for anyone seeking transparency, accountability for revenue flows, or simply the honest and straightforward conduct of government business. Trying to block fraudulent oil marketers from access to government oil subsidies, pushing for accountability for revenues due to the Federation from the oil and gas sector, managing competing sectoral interests, and dealing with the noxious politics surrounding the sector have meant stepping on many powerful toes.

Dr. Okonjo-Iweala described her efforts to bring transparency and accountability to the sector as "probably one of the most stressful and dangerous tasks of my job as Finance Minister."[57]

These observations are consistent with the conclusions reached by Nicolas Shaxson in an earlier analysis of efforts to improve transparency in Nigeria's oil and gas sector. He traced poor governance outcomes to two features of the "resource curse," the paradox that countries with abundant natural resource wealth tend to have worse development outcomes than countries with few resources. The first feature of such countries is that because the rulers get revenue from extractive companies rather than taxing their citizenry, the latter are disempowered; the second is that the revenues "foster the politics of patronage, involving fragmentation of society and the political system."[58]

V. Concluding remarks

First, a recap of the facts: Capital flight exists. Few would deny its existence, notwithstanding that some methods of identification remain contentious. This paper has given examples and discussed some of the major controversies. There is also widespread recognition of, and concern about, asymmetries in mirror trade statistics as discussed here. Much of the debate in the literature on trade data asymmetries is about the extent to which they can be attributed to capital flight. The scale of discrepancies in some cases is such that if they indeed arise from capital flight, the implications are staggering and embarrassing. It defies comprehension as to how such systematic haemorrhaging can be allowed to persist in economies

[57] Ngozi Okonjo-Iweala, *Fighting Corruption is Dangerous: The Story Behind the Headlines*. Cambridge, Massachusetts: The MIT Press, 2018, p. 54.

[58] Shaxson, Nicholas (2009) *Nigeria's Extractive Industries Transparency Initiative. Just a Glorious Audit?* London: Chatham House. Online at https://www.chathamhouse.org/sites/default/files/public/Research/Africa/1109neiti.pdf, accessed on 22 July 2019.

desperately seeking development capital. These tacit implications explain the sometimes-acrimonious nature of the debate. While not all asymmetries in mirror trade data can be ascribed to capital flight, there are persuasive reasons to seriously consider the likelihood that much of them can.

Poor data governance, both nationally and globally, has contributed to ambiguities surrounding the analysis of commodity-trade enabled capital flight. By fanning the flames of controversies around identifying capital flight, the weak state of data integrity effectively renders data governance itself an enabler of capital flight. The politicians who make the formal rules may also be interested parties in the game. Therefore, any credible data regime should consider independent verification systems and processes to mitigate conflicts of interest. To the extent that international agencies rely on national government agencies for data, such datasets are as reliable as the integrity of the primary sources that may or may not be self-interested players. But if states stand by their data, they should accept the valid conclusions therefrom.

The sustainability of capital flight depends on the relative ease with which "dirty money" obtained by illicit means can morph into clean money. Illegitimate wealth has the undesirable characteristic of being troublesome to spend. Money laundering thus is a necessary adjunct to dirty money, without which the pursuit of illegitimate wealth would cease to be a worthwhile venture. Money laundering is the gamut of steps by which illicit wealth is given the appearance of legitimacy so that the owner can enjoy it as if it was clean. This process is simplified in Figure 1, depicting the money laundering criminal enterprise proposition. Anti-money laundering (AML) measures refer to the repertoire of mechanisms by which society attempts to prevent criminals from having unfettered access to the clean transform of their money. Factors that weaken AML measures promote capital flight.

Capital flight has been ongoing for decades in Africa.[59] Institutionalizing capital flight and keeping it going for an appreciable period is likely to have entailed displacement of some existing opposing structures and blockage of new ones.[60] Good governance is inimical to capital flight, and poor governance is conducive to it. In other words, capital flight is antagonistic to proper institutions for good

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[59] James K. Boyce and Léonce Ndikumana, 'Is Africa a Net Creditor? New Estimates of Capital Flight from Severely Indebted Sub-Saharan African Countries, 1970-1996,' *Journal of Development Studies,* Vol. 38, No. 2, 2001.

[60] For an out-of-Africa example of how institutions can be assailed, see McMillan, John, and Pablo Zoido. *2004*. "How to Subvert Democracy: Montesinos in Peru." *Journal of Economic Perspectives*, 18(4): 69-92.

governance, instead promoting self-serving and expedient forms of governance. Capital flight can undermine an institution by altering its components, limiting its scope, diminishing its intensity, and thereby negating its efficacy. Thus weakened, the resulting institutions are able, and indeed intended, to accommodate capital flight and promote opportunistic crimes.

Here is how Mr. Femi Falana, a Senior Advocate of Nigeria and a distinguished human rights advocate has described the enabling environment for kleptocracy and its opportunistic complements in Nigeria:

> Abacha's son was charged with stealing NGN463bn.[61] The case was in court for 14 years…. He said the immunity of his father should be extended to him. The Supreme Court said even if your father were still alive, he would have lost his immunity. But the objection was taken to court for 14 years. By the time they came back, the witnesses could no longer be found, the judge had been promoted, so you have to start *de novo*, and the case was withdrawn.
>
> Today in England, if you file a motion that is meant to delay the case, you are disciplined by the law society…. But here, these are the lawyers that we are celebrating.
>
> [Take] the case of James Ibori [former governor of Delta State accused of financial crimes]. Without a trial, he was discharged and acquitted. The judge carelessly forgot that the $15m seized from him when he wanted to bribe former [Economic and Financial Crimes Commission] Chairman Nuhu Ribadu was still there as an exhibit….
>
> When the same man got to England, he pleaded guilty. You know why he pleaded guilty? When the lawyers saw his defence, they told him it was a sham and they could not go on with the case. He asked if they could not file an appeal, and they told him, 'We don't do that here.' They told him that if they went on and he got convicted, he would get the highest punishment. But that is not the real problem. They told him they were afraid they would also lose their licence to practice law because they would be charged for wasting the resources of her majesty's court.[62]

"To own the fight"

In December 2017, staff of Nigeria's EFCC staged an "anti-corruption walk" to mark International Anti-Corruption Day, calling on the Nigerian people "to take ownership of the fight against corruption."[63]

[61] This sum is equivalent to approximately US$1,2 billion. Abacha's son refers to the son of the military ruler of Nigeria from 1993 to 1998, General Sani Abacha.

[62] Samson Folarin, "Falana Laments Corruption in Judiciary, Seeks Reforms," *Punch,* April 17, 2019. Online at https://punchng.com/falana-laments-corruption-in-judiciary-seeks-reform/, accessed on 24 July 2019.

[63] Paul Obi, "Nigeria Facing Adverse Effects of Corruption – EFCC," *The Day* (Lagos), December 12, 2017. Online at https://allafrica.com/stories/201712120226.html, accessed on 24 July 2019.

The call "to own the fight" is a plea for citizens to get involved. Institutions are the instrumentality for citizen engagement, the result of the complex chemistry between formal and informal rules that define a country's incentive structure. The formal rules originate from the state, and the informal rules are created by the people. As this study has shown, trade-related capital flight is rooted in the way in which governance has been bent to serve this purpose. Governance is neither self-implementing nor regenerative, meaning that it does not run itself or repair itself when broken. If the people do not get involved by investing in the task of governance through playing their roles, they may not experience good governance regardless of how sanguine their expectations are. The people will have to take charge and reshape governance by fixing institutions. This imperative is aptly captured in historical perspective by Roger Myerson in his Nobel Prize Lecture in 2007.

> Economics began with Xenophon's "Oeconomicus" (c 360 BCE), in which Socrates interviews a model citizen who has two primary concerns. He goes out to his farm in the country to monitor and motivate his workers there. Then he goes back to the city, where his participation in various political institutions is essential for maintaining his rights to own this farm. Such concerns about agents' incentives and political institutions are also central in economic theory today. But they were not always.[64]

A committed state will ensure that what occurs is adherence instead of malfeasance; action instead of inaction and dysfunction. It will respond diligently to whistle-blowers and credible informants, and cultivate intelligence rather than ignore the feedback or alarms from the public. When feedback is ignored, and the formal system is perceived as a sham, the public will not be motivated to feed the state with intelligence.

Establishing a functional public protector may be as much a necessary adjunct to good governance as money laundering is a necessary adjunct to capital flight. Establishment of prosecuting authorities for economic crimes no longer appears to be sufficient commitment to antigraft, especially when kleptocrats enjoy immunity from prosecution while in office. Furthermore, many of the anti-corruption agencies lose credibility as they become *de facto* instrumentalities of incumbents, employed deftly against opponents and skewing political competition by inducing opponents to defect to the ruling party to gain respite through prosecutorial discretion. Such carpet-crossing by politicians amplifies incumbency

[64] Myerson, Roger B. (2008) "Perspectives on Mechanism Design in Economic Theory," *American Economic Review* 98(3), p. 586.

advantages, and corrodes the political competition necessary for accountability and continued relevance of the electorate. In short, it corrodes democracy.

As of this writing, the initiative of UN Comtrade to provide users with more information does not appear to be moving at an encouraging pace. The initiative is a vital one, as it promises to provide details on the nature of trade flows and partner-country attribution, especially re-exports, re-imports, goods for processing, and intra-firm trade, thus allowing for better analysis of bilateral trade asymmetries. Regrettably there are no specific member-states championing the initiative, a troubling situation given the entrenched interests in support of the status quo.

"Gold is a country," as declared by the South African authorities, is a poignant illustration of the possibility that what some observers see as mere data imperfections may in fact be manifestations of an calculated design. If so, why would the Government wish to change? The decision by the South African government to conflate gold exports categories following the 2016 UNCTAD report is an illustration of the widespread resistance to change and transparency. Why the extraordinary dispensation to this single commodity? Our analysis has clearly documented the fact that the problem is not only of defective rules and procedures, but also about rule violations that go unpenalized. Who is to enforce the rules *when the ghost buster is the ghost most of the time*?

Regarding the analogy between free ports and bank secrecy jurisdictions, the key question that must be asked is the scope of responsibility expected of the governments of countries that host these free ports. It is relevant to recall that Swiss banks would have resisted transparency reforms if the US and Europe had not pressured Switzerland to reduce bank secrecy. So, who will pressure the governments of countries hosting opaque trading hubs to open up? Who is interested in pushing for timely implementation of the UN Comtrade data system upgrade? Put differently, who are the winners of the global criminal enterprises value chain? We know who the losers are.

There have been some notable achievements worldwide to increase accountability and reduce injury to commodity dependent countries who are predominantly developing nations. The Eextractive Industry Transparency Initiatives discussed above address accountability issues in fuels and minerals. The Kimberly Process Certification Scheme to combat blood diamonds, in conjunction with subsequent US legislation, Dodd-Frank Section 1502 on conflict minerals, aim to address similar concerns in the solid-

minerals subsector.[65] So far, there is no equivalent initiative for cash crops. The underlying theme in these initiatives is the importance of transparency of transactions and responsible corporate citizenship. It is time to demand that nations hosting trading hubs join the global responsibility movement by promoting transparency in international trade.

[65] See Melvin Ayogu. and Zenia Lewis (2011) "Conflict Minerals: An Assessment of the Dodd-Frank Act," https://www.brookings.edu/.../conflict-minerals-an-assessment-of-the-dodd-frank-act/, accessed on 3 October 2019 for an elaboration of the conflict minerals legislation.

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Appendix: Practitioner Narrative of the South African Exporting Experience

The International Trade Department exported **15,144** shipments to 15 non-RSA countries for the year ending June 2016.

However, the figure does not communicate the intricate and at times laborious documentary processes that are required to facilitate this trade. The process is further complicated by the fact that there are on average between **300** and **600** individual articles on each shipment. As certain products are governed by legislative requirements, these products will require individual certification or documentation at different stages throughout the supply chain.

There are **3** main groupings of certification required:

- **Vendor** certification
- **Export** certification from South Africa
- **Import** certification into the relevant non-RSA country

Each of the above groupings requires their own sets of documents to allow goods to move between countries.

Documentation requirement per grouping:

Vendor Certification

- ✓ Material Safety Data Sheet
- ✓ Movement Certificates
- ✓ Certificates of Analysis
- ✓ Laboratory test sheets
- ✓ NRCS certificates

Export Certification

- ✓ PPECB certificates
- ✓ Hazardous Declarations
- ✓ Transport Documentation
- ✓ Custom Documentation

Import Certification

- ✓ In-Transit Permits
- ✓ Phyto sanitary certificates
- ✓ Import Permits
- ✓ Fumigation certificates

Please allow me to briefly outline the extent of the abovementioned requirements by using the example of a single shipment recently dispatched from **South Africa to Angola**.

	Nr of Documents	Nr of pages
Vendor	6	29
Export	24	506
Import	21	66
Total	51	601

10 – 15 days lead time

The table above illustrates the number of documents that was required to move this one shipment to Angola. International Trade dispatched 1262 shipments to Angola for the year ending June 2016, that equates to **64,362** numbers of documents and **758,462** number of pages.

In obtaining each and every document and certificate, specific requirements need to be met; which invariably adds to the time it takes to place those products on the shelves. Should the documentary requirement reduce, then the current time taken should follow.

Bear in mind that the above example did not include the SADC requirements. If the country had done so, additional documents would have been added and below table illustrates the increase in number of documents:

	Nr of Documents	Nr of pages
Total Non SADC Load	51	601
Plus:		
SADC invoices	+ 4	+ 5
SADC Certificates	+ 28	+ 28
Total	83	634

10 – 12 days lead time

Over and above the number of documents and the time these take, there is the additional and quite archaic manual practice where **3** different stages of progression through **3** different SARS teams are required to obtain approval. These stages consist of:

- Bill of Entry & Date number (physical addition to certificate)
- 3 stamps (3 different teams)
- 2 signatures (2 different teams)

The impact of this system can be seen in the average monthly figures below:

Impact of SADC per month (Average)	
SADC shipments	**114**
Certificates	**3,207**
Signatures	**6,414**
Stamps	**9,621**
Pages	**54,570**

Below is an example of export documentation per shipment:

In the case of road freight through multiple borders, a set of Customs documents, which forms part of the Export documentation, is required per border post. This can triple the number of Customs documents required per shipment.

The numbers above clearly illustrated an untenable situation, more so in light of the planned growth that we have planned for the rest of Africa.

Vendor Certification			
Certificate	**Regulatory body**	**Product**	**Reason**
Material Safety Data Sheets	South African National Standard (SANS)	All Products classified as Hazardous for transport e.g. aerosols	Advice shipper of the effects of usage of product, hazardous evaluation related to the product's handling, storage, transportation and emergency procedure in case of an accident.
Movement certificates	State Veterinary (Department of Agriculture Forestry & Fisheries)	All Animal-based products being moved between Provinces	Determination of products' origin
Certificates of Analysis	Nationally accredited Laboratories	All Food Products	To attest the quality of exported commodities
Laboratory test sheets	Nationally accredited Laboratories	All Food Products	To attest the quality of exported commodities
NRCS certificates	National Regulator for Compulsory Specifications (NRCS)	Canned & Frozen Fish &Electrical products and appliances	Surveillance through inspection to monitor compliance with compulsory specifications

Export Certification			
Certificate	**Regulatory body**	**Product**	**Reason**
PPECB certificates	Perishable Products Export Control Board (PPECB)	Perishables, Canned Vegetables & Fruit, Maize Meal, Chicken	Quality certification & cold chain management to support the export competitiveness of RSA perishable products.

Hazardous Declarations	Shipper	All Hazardous Products	Certification that hazardous goods have been packed labelled and declared in accordance with the standard international shipping regulations for transport.
Transport documentation	Shipper	All Products	Forms part of Proof of Delivery (POD) documents.
Customs documentation	SARS	All Products	Customs clearance at various border posts.

Import Certification

Certificate	Regulatory body	Product	Reason
In-transit permits	State Veterinary Department in Countries of transit	Permit applicable products	Permission for regulated stock to pass through a country to final destination.
Phytosanitary certificates	DAFF (Department of Agriculture Forestry & Fisheries)	All Plants Products	Assurance that RSA complies with all international Phytosanitary standards in the prevention of the spread of pests and diseases of plants and plant products.
Import permits	Importing Country	As stipulated by Importing Country	Issued by a National government authorizing the importation of regulated goods into its territory.
Fumigation certificates	Importing Country	As stipulated by Importing Country	Assurance that pests, termites or any other harmful living organisms have been eliminated, to prevent transfer of these.

Note: The source of the South African byzantine experience is Mangozhe, Gwarega (2017) “Monograph on Intra African Trade Champions.” Presentation to the Afreximbank Roundtable Discussion for Intra African Trade Champions (INTRA-CHAMPS), Kigali, Rwanda, 30 June.