Symposium on IFFs: Illicit Financial Flows and the Real Estate Sector in Africa

By:

Irene Kariuki

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Introduction

The exponentially growing discomfort around Illicit Financial Flows (IFFs) globally is an indicator of the undesirable effects that result from the IFFs, ranging from social, economic and even political consequences. There is a general concurrence that IFFs take away substantial amounts of finances from the developing countries, which finances could otherwise be utilised in domestic investments, provision of public services such as education, security, health etc., and offsetting foreign debts. It is on this basis that discussions about IFFs in developing countries should not be postponed.

IFFs are defined as monies illegally earned, transferred, or used. According to the UNCTAD–UNODC Task Force, the core elements for the definition of IFFs are: illicit origin, transfer or use, exchange of value instead of pure financial flows, flow of value over time, and flows that cross borders. IFFs take four specific forms, namely illicit tax and commercial activities; illegal markets; corruption and theft-type activities; and terrorism financing. The common end goal for all these forms of IFFs is to conceal the illicit proceeds, and the methods by which these proceeds are obtained, from the public and the law enforcement institutions. This concealment is achieved through the process of money laundering.

The real estate sector has become a convenient avenue to launder money. In this blog, I examine how the real estate sector facilitates IFFs in Africa. I further seek to identify some of the control measures that can be put in place to combat this form of abuse in African countries.

Money laundering as a form of IFFs

The definition of money laundering has evolved over the years. At the time when the word was invented, money laundering was considered to entail the act of cleaning dirty money, through businesses such as car washes and laundromats, to conceal their illegal sources. While “cleaning money” is still the substratum of money laundering, there has been a push to refer to money laundering as an IFF, in order to include the act of concealing both the origin and the intended use of the illegal money. Money and activities that have a clear connection with illegality, such as corruption and money laundering among others, fall under IFFs, according to the World Bank. Accordingly, this blog propounds that IFFs should be defined more broadly to include money laundering. This is because money laundering, being a financial crime, is technically not only an IFF itself, but it is also grounded on illicit activities which result in IFFs.

The Real Estate Sector and IFFs

The real estate sector is considered as one of the oldest sectors through which money laundering easily thrives, particularly because of the ability to launder and move large amounts of money in single transactions, and because the subject property can be used as a source of supposedly “clean” income through further transactions such as leasing the properties out. This blog advances the argument that money laundered through channels other than financial institutions is often placed in sterile investments such as real estate, in concurrence with the sentiments of Brent L. Bartlett of the International Economics Group Dewey Ballantine LLP. Sterile investments are investments that only generate revenue to the investor when they are disposed off for more than the purchase price, thus generating limited additional value to the broader economy.

While this blog focuses on the real estate money laundering problem in Africa, it is worth keeping in mind that the real estate money laundering is not unique to the African countries. It is a global problem, and through globalization, the world has become interconnected, making it easy to move funds across borders. For example, in a report by the Global Financial Integrity (GFI), more than $2.3 billion was laundered through US real estate from 2015 two 2021. Similarly, and to further back the fact that real estate money laundering is a global problem, in the case of Daniel Ford & Co. Ltd., a company was reported to have catered to several Nigerian politically exposed persons (PEPs), and two Nigerian businessmen allegedly conspired to bribe former Nigerian petroleum minister Diezani Alison-Madueke by purchasing real estate in and around London for her benefit.

The same company was linked, by the Pandora Papers investigation, to a former Nigerian minister, Stella Oduah, who secretly acquired real estate properties in London, concealed behind an anonymous company registered offshore.

The situation in Nigeria is another good example of the real estate money laundering problem facing African countries. Prof Bolaji Owasanoye, the chairman of the Independent Corrupt Practices and Other Related Offences Commission (ICPC), noted that the real estate is a key sector in the laundering of IFFs due to the minimal regulation in the sector, during a capacity building workshop organized by the ICPC. He further illustrated the spread of real estate money laundering across Nigerian major cities such as Lagos, Abuja and Port-Harcourt.

That being said, this blog emphasizes that if African countries are to succeed in their efforts to prevent or control money laundering in the real estate sector, international cooperation is critically important.

Factors Promoting Generation of IFFs in the African Real Estate Market

There are several drivers that encourage IFFs both in Africa and beyond. In Africa, the players in the IFFs take advantage of the major policy and governance gaps, inadequate regulation in the financial and non-financial sectors and the glaring institutional incapacities. Sector-specific factors, such as the ability and ease to launder money in some sectors than others, also play a major role in enabling IFFs.

In most African countries, corruption is one of the major challenges affecting the real estate sector. There are also highly inadequate land administration and management processes, which are largely manual in nature, and this presents an opportunity for abuse, thus aiding laundering of illicit finances through the real estate sectors. The real estate sector in most African countries is also largely unregulated, with inadequate or no anti-money laundering regulations to ensure transparency and accountability in real estate transactions. Therefore, there is less scrutiny by the government agencies responsible for fighting money laundering.

Professionals, including the lawyers and real estate agents, and businesses that operate in the non-financial sector which enjoy minimal or no regulatory audits also enable IFFs in the real estate sectors in Africa. These professionals, especially lawyers, are used in the various stages of the process of money laundering to create corporate vehicles, bank accounts, transfer proceeds, purchase and sale of property, and craft clever ways to bypass anti-money laundering regulations. Lawyers also use rules of attorney-client privilege to protect the identities of the persons involved in the IFF activities.

Additionally, the lack of information sharing and co-operation between regulatory institutions hinders the effective regulation and provides a loophole to the advantage of the criminals.

Recommended Way Forward

Some countries in Africa have already kicked off the regulation of the real estate sectors, in a bid to curb money laundering and IFFs. For instance, the Republic of South Africa has stern anti-money laundering laws in the real estate sector and the Financial Intelligence Centre is responsible for combating money laundering and ensuring compliance with anti-money laundering laws. The Republic of Kenya also has in place robust anti-money laundering laws and institutional framework including the Financial Reporting Centre, to curb money laundering and ensure compliance with the anti-money laundering laws.

Given the far-reaching impact of IFFs in African countries, and further, given that the real estate sector is a common breeding ground for the IFFs, it is critical that necessary actions be taken towards regulation of the sector.

First, governments should implement comprehensive anti-money laundering laws that specifically address the real estate sector. This would help in gaining control and oversight over the real estate transactions and discourage its use as a safe investment haven for IFFs criminals. These laws should have measures such as mandatory customer due diligence, mandatory reporting responsibilities in case of suspicious transactions and mandatory disclosure of beneficial ownership information for the entities involved in the transactions. On a positive note, there has been a wave of enactment of beneficial ownership regulations in Africa in the recent past. For example, Tanzania and Kenya have both recently enacted robust regulations to facilitate the disclosure of beneficial ownership in companies registered and carrying on business in the countries. This information is also used by the anti-money laundering agencies in their investigations.

Second, governments should enhance and empower regulatory bodies to oversee the real estate sector. Inter-institutional collaboration should also be encouraged to facilitate information and intelligence sharing among the different regulatory bodies and law enforcement agencies in the sector.

Another important action that governments should take is to create awareness among the players in the real estate sector, to educate them on the ways through which the sector is used by criminals in IFF activities, and the tools that can be used to mitigate the risks that arise therefrom. The players in the sector should also be educated on their responsibilities, including identifying and reporting any suspicious transactions. Mandatory registration and licensing of the players in the real estate sector can also help in enhancing regulation of the sector.

The consequences and penalties for involvement in IFF activities should be dire enough to make it less attractive to criminals. This could be in the form of punitive fines and longer prison sentences.

Finally, the use of technology to develop more efficient and transparent land administration processes can help combat corruption and create transparency in real estate transactions. With digitization, physical interactions, waiting time and costs incurred in the processing of land transactions are largely reduced, and this translates to reduced need to incentivize the land cartels. A similar outcome has been seen in other countries that have embarked on digitization of land records, such as Rwanda. Apollinaire Mupihanyi, the Executive Director of Transparency International Rwanda, noted that "*although we can't say that with digitalization all issues were solved, I ascertain that corruption was drastically reduced*." Kenya has also embarked on a land administration digitization journey, aimed at integrating all operations of the departments of the Ministry of Lands and Physical Planning and provide a turnkey operation where end-to-end transactions in relation to land are conducted. Additionally, Ghana recently enacted an e-conveyancing law, to facilitate the digitization of conveyancing transactions.

If these examples, among others, are anything to go by, there is hope for African countries to follow suit and use technology to curb corruption and enhance detection of money laundering activities in the real estate sector. If these recommendations are implemented, African countries can reduce the prevalence of IFF activities in their real estate sectors and improve the integrity of their real estate markets, which would be a win-win for them.

Conclusion

The contribution from the real estate sector to the development of African economies cannot be downplayed. For example, Kenya's real estate sector accounts for approximately 7.5% of the country's Gross Domestic Product. After all is said, the real estate sector is certainly a weak link in the fight against IFFs in Africa and governments and policy makers should take action to enable them detect and combat IFF activities in their respective real estate sectors. This can be achieved through collaboration with the private sectors and the professional bodies such as law societies.

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