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AS tax collection is widespread; businesses and government officials pay the group. The group's tax collection is more efficient than the FGS and the FMSs.

A Losing Game:

Countering Al-Shabab's
Financial System

Hiraal Institute

Hiraal Institute seeks to be the premier security think tank in Somalia. Building on the security experience of its members, it aims to promote security throughout the Horn of Africa and usher in a peaceful Somalia.

Hiraal Institute

Mogadishu, Somalia

www.hiraalinstitute.org

info@ hiraalinstitute.org

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Introduction

Much has changed since Hiraal Institute's 2018 report on the AS financial system.¹ The group's capability in tax collection has improved, and complaints about the group's reach have been growing ever since. This study was therefore done in order to understand how the group has been faring since then, what the government's reactions have accomplished, and what can be done in order to curb the group's financial operations.

The findings in this study are based on interviews conducted from June to October 2020 with 70 businessmen, government employees, and NGO representatives in Mogadishu, Southwest State, HirShabelle, Jubbaland, and Puntland . In addition, Al-Shabab officials were contacted in order to understand the process from the group's perspective. We considered these as sufficient to give us the general picture of the AS tax collection across Somalia. The interviews were conducted in person; only the interviews with AS were conducted by telephone. Information that is best suited for the eyes of policymakers is included in a separate, more elaborate, document.

AS taxes all major companies; these taxes are in the form of annual Zakah and monthly payments.² Clans and businesses in AS areas are also made to pay *Infaaq* when the local AS government is short in cash.³ The group has substantial money reserves, making it the only Somali polity that has achieved this impressive feat. While tax collection increases yearly, salaries have not changed, and military operations by the group have not increased. This means that, by all measures, the group is running a major financial surplus. The version of this paper edited for policymakers will shed light on where the surplus money is going.

Paying of taxes to AS is not a voluntary endeavor, with an almost universal desire among taxpayers to be taxed solely by the Somali government. Fear and a credible threat to their lives is the only motivation that drives AS taxpayers. The business environment is difficult for businesses in Somalia: the government's failure to monopolize violence in the areas it controls is directly responsible for AS' success in collecting taxes from here. The businesses complain that they are victims of a government that has put them in their current position of paying two parallel governments.⁴

¹ See "The AS Finance System", *Hiraal Institute*, 2018, URL: <https://hiraalinstitute.org/the-as-finance-system/>

² AS official in Marerey, Aug 2020.

³ Ibid.

⁴ Businessman in Mogadishu, Oct 2020.

A comprehensive approach is needed to dismantle the group's financial system and in a manner that does not unnecessarily hinder private business. The current government approach is counterproductive in achieving its aims and ineffective in hindering AS tax collection. This paper shows how an all-government approach is needed to tackle this issue, in collaboration with the business community.

Businesses that pay AS

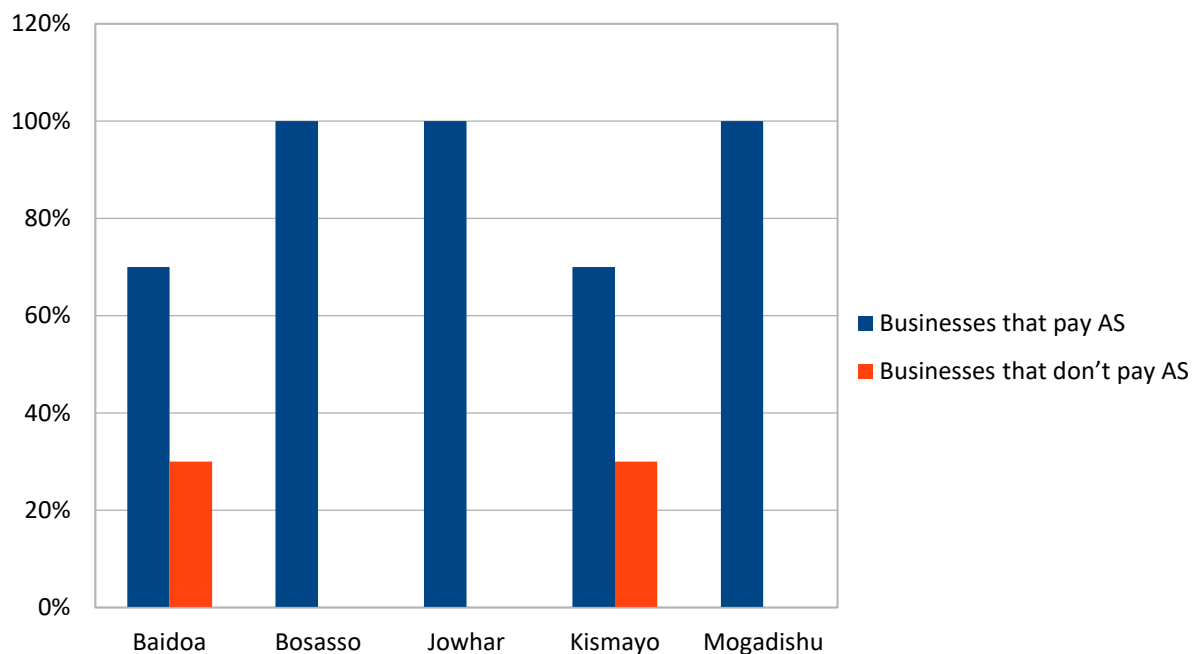


Figure 1 Surveyed businesses that pay AS and those that do not (Ten in each city)

The tax collection by AS is enabled by little or no security protection afforded to businessmen in much of the country. Its punitive operatives are active in almost all areas of Mogadishu, including the Villa Somalia neighborhood; most of Bosaso and Jowhar; and, to a lesser extent, much of Baidoa and Kismayo. Consequently, businesses in areas where it is difficult for AS to operate are more likely to reject its demands to pay taxes. While the group calls and threatens businessmen in these areas, more are likely to reject their demands, especially if they have no business interest in AS areas or do not need to pass through them.⁵

⁵ Importer, Kismayo, Jul 2020.

All the major companies in southern Somalia pay the annual *Zakah* to AS; only very small-scale businesses such as street hawkers that have not reached the *Zakah* requirement are untaxed by the group.^{6 7} However, some businesses in AS territory that do not pay the *Zakah* pay a monthly tax to the local AS authorities.⁸ Businesses are taxed at the port; their cargo is taxed in transit, with the cargo truck being taxed separately; they are also taxed annually 2.5% of their accumulated wealth; agricultural produce is taxed at harvest time and again when being sold.⁹

AS taxes everything in the territories it controls; it is so specialized that farmers are not allowed to use the river and its canals unless they pay special taxes for irrigation of farms.¹⁰ Likewise, it is rare to find a businessman refusing to pay AS taxes in contested areas where the group has an active military or security presence; such a business would have to be in an area where the group has no ability to conduct operations.¹¹ Tax refusal is not an option in areas controlled by the group; everyone pays taxes.¹²

Combined FGS and FMS road taxes cost less than AS taxes; however, cargo truck operators prefer paying AS because it is a one-time payment at a checkpoint where they are issued a receipt that secures travel through the group's territory, which is most of the countryside.¹³ The AS taxation system is more advanced and widespread in the relatively new FMS states such as HirShabelle where the group is aware of and taxes all transactions of private real estate.¹⁴ The government's taxation system is so informal and disrespected that a government official that had paid AS \$800 talked his way out of paying the government taxes for the same transaction for which he had paid the AS taxes.¹⁵

AS is able to assess tax obligations of businesses because importation manifests are provided to it by government employees, especially those that work at the seaport; AS uses this detailed

⁶ AS official in Jamame, Aug 2020.

⁷ *Zakah* is paid annually of one's liquid assets, including cash savings and inventory in a shop/warehouse that one intends to sell. Personal items and properties are not covered under *Zakah*.

⁸ AS official in Jamame, Aug 2020.

⁹ Electronics importer, Mogadishu, Jul 2020, NGO official, Mogadishu, Aug 2020, and AS official, Jilib, Aug 2020.

¹⁰ AS official in Fidow, Jul 2020.

¹¹ AS official in Jamame, Aug 2020.

¹² Ibid.

¹³ Cargo truck operator, Jowhar, Aug 2020.

¹⁴ HirShabelle official, Jowhar, Aug 2020.

¹⁵ HirShabelle official, Aug 2020.

information to demand customs taxes of all imports.¹⁶ Businesses confidently pay AS taxes because they expect AS to heed its part of the deal as it has always done; those that pay taxes are free to go wherever they want, while those that refuse are punished and their lives are endangered.¹⁷ The punishment, before any death threats are made, ranges from fining them hefty amounts to restricting their access to markets.

Due to the volume of money going into real estate, AS heavily taxes this industry. It is almost as closely watched by the group as the importation business. AS is aware of almost all transactions; realtors are called by the group, “given details of the transactions they conducted, and ordered to pay a non-negotiable amount, and they pay exactly what AS demanded”.¹⁸

How AS collects taxes

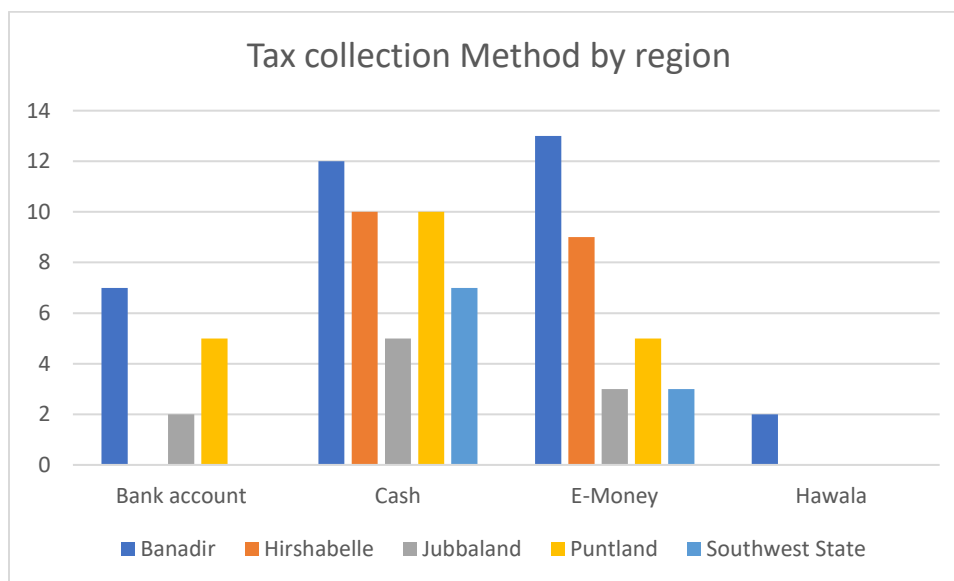


Figure 2 Respondents' Tax Payment Methods

AS uses one mobile number to contact traders in any given area during each collection period.¹⁹ Traders unsure whether it is AS that is contacting them usually contact their kinsmen in the group to confirm the credentials of the caller before heeding their instructions.²⁰ Taxes are

¹⁶Importer, Kismayo, Jul 2020.

¹⁷Livestock trader, Kismayo, Jul 2020.

¹⁸Realtor, Kismayo, Jul 2020.

¹⁹Civil servant in Jubbaland, Kismayo, Jul 2020.

²⁰Civil servant in Jubbaland, Kismayo, Jul 2020.

collected in various ways, depending on the amount being collected and the place where the business is based. In areas controlled by the group or contested areas where the *Amniyaat* has freedom of operations, tax collectors go directly to businesses and demand payment.²¹ The group uses clever tactics to restrict the movement of its money, and the group is largely able to circumvent much of the current measures in place to dent its tax collection.

While some of the payments to AS are done by depositing the funds into bank accounts, the banks are complying with the existing regulations. The account holders provide IDs as required by law, and they report suspicious and large transactions. The major Somali financial institutions, including banks and hawalas, have been complying with the regulations set by the FRC/CBS in accordance with the AML-CFT law, according to the DG of the FRC.²²

How much AS collects in taxes

Monthly tax collected by the group amount to at least \$15M, more than half of which comes from Mogadishu.²³ Based on how widespread the group's taxation is, and how much more depth it has compared to the FGS and the FMSs in southern Somalia, we assess that this amount is a very conservative estimate. Whereas the government's and the group's tax formulas are largely similar; however, in addition to the sources of revenue that it shares with the government, it has types and sources of taxes that the government does not have. The 2.5% annual *Zakah* on accumulated wealth, the taxation of agricultural produce, and the taxation of land sales and development are exclusive to AS and are as substantial as the port collections, which is the government's main source of taxes.²⁴

How AS deals with those that refuse to pay taxes

Virtually all businessmen interviewed for this study considered AS taxes as harsh, unfair, and illegitimate. One major taxpayer referred to AS taxation as the work of a "Mafia group that has left any pretenses of being an Islamist group".²⁵ The group is brutal in its tax collection; a farmer

²¹ AS official in Fidow, Jul 2020.

²² Amina Mohamed, DG of the FRC, Oct 2020.

²³ AS official in Fidow, Jul 2020; AS official in Jilib, Jul 2020; and AS official in Kurtunwaarey, Jul 2020.

²⁴ While the government has land taxes, it is negligible and rarely collected.

²⁵ Businessman in Mogadishu, Sep 2020.

complained that he was being forced to pay operations taxes for his tractor even when it is out of operation due to technical issues.²⁶

Individuals refusing to pay AS are forced to shut down their business, change their contact information, or flee the country.²⁷ This pressure is only bearable to individuals who live away from the reach of AS. Sometimes, AS may force businesses to pay the taxes of previous years under which the business was not registered for them. Newly registered businesses are forced to pay the taxes of current and previous years.²⁸ In extreme cases, when the taxpayers blatantly refuse to pay what AS decides is owed to it, it carries out targeted killings of the business owners who refuse to comply with its demands. Given this reason, most business owners see that it is in their interest to pay AS taxes.²⁹

Government officials paying AS taxes

Illustrating how widespread payments of AS taxes are is the payment of taxes to the group by government officials, including top commanders of the SNA that are not in direct danger from the group. The episodes cited below show that payment to AS has little to do with recognizing the legitimacy of the group, but more to do with the practicality of real life, which makes it impossible to conduct business in areas where the group has operational presence. On the other hand, this act of taxing government officials and not banning their businesses shows that AS is a rational actor that chooses its battles wisely. Had the group chosen to ban government and pro-government businesses from functioning, sentiments would have soured against it at a much greater magnitude than it already has without gaining it anything in return.

There are some government officials that give AS a part of their salaries so as not to be targeted by the group.³⁰ Similarly, some government contractors in the private sector pay AS taxes in order to protect their business interests within AS territory and contested areas where the group is active.³¹ Some government employees pay AS income taxes, in the hopes that the group may spare them.³² Likewise, government officials that have businesses pay AS in order to secure the

²⁶ Farmer in Jowhar, Jul 2020.

²⁷ Civil servant, Mogadishu, Jul 2020.

²⁸ General merchandise importer, Mogadishu, Jul 2020.

²⁹ Restaurateur, Mogadishu, Aug 2020.

³⁰ AS official in Jamame, Aug 2020.

³¹ Civil servant in Jubbaland, Kismayo, Jul 2020.

³² Civil servant in Jubbaland, Kismayo, Aug 2020

freedom their commercial operations.³³ Similarly, AS imposes a \$1000 registration fee to local government officials whenever they register pieces of land.³⁴

The case of an SNA commander paying AS is so interesting that it deserves to be quoted in full:

“We sometimes encounter situations where we are forced to pay AS taxes. Let me share with you a story about sending money to AS despite being at war with it. I started to build a house for myself last month. The engineer that was constructing the house for me told me that he is receiving regular calls and threats from AS to stop the construction activity or to collect the due tax from the landlord. I refused to pay the money because I am not in fear of AS. Days later, the construction activities stopped as the engineer left the job. I hired another engineer immediately, but the new engineer received the same threats as the previous one. The vehicles that were transporting construction materials for my building were also forced to stop transporting the materials for me. Finally, I was forced to either drop the construction work or to pay AS taxes. Regrettably, I paid \$3600 to them, and my house was completed”.³⁵

AS services provided to taxpayers

AS resolves disputes among the businesspeople, especially when a business files a complaint against other businesses. Because the group taxes exports at a scale unlike the FGS/FMSs and provides, in return, some essential services to exporters. For instance, it regulates the production of certain export products such as lemons and ensures that the quotas set by farmers' associations are not exceeded.³⁶ Another vital service is the security guarantees to its taxpayers; taxes paid at any of its checkpoints ensure safe passage along its territory, and also safety in the areas of active military operations held by the government.

However, businesses complain that the above is not commensurate with what they are forced to pay. The services are not considered to be worth the high taxes paid by the traders, as can be seen from the below result of the interviews with the traders.

³³ AS official in Fidow, Jul 2020.

³⁴ Land registrar, Mogadishu, Jul 2020.

³⁵ SNA commander, Mogadishu, Jul 2020.

³⁶ Lemon exporter, Jowhar, Aug 2020.

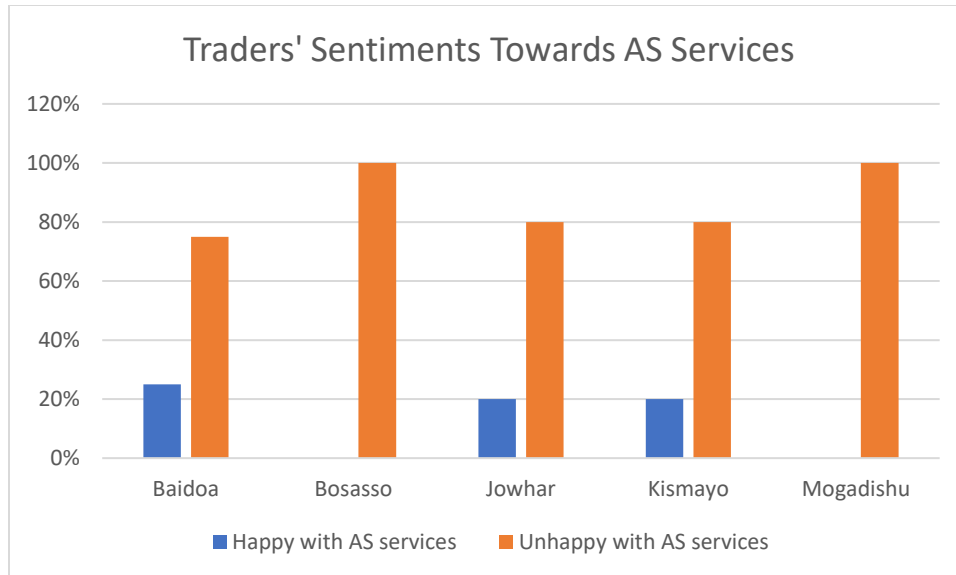


Figure 3 Traders on if they are happy with what they get in return for paying AS taxes

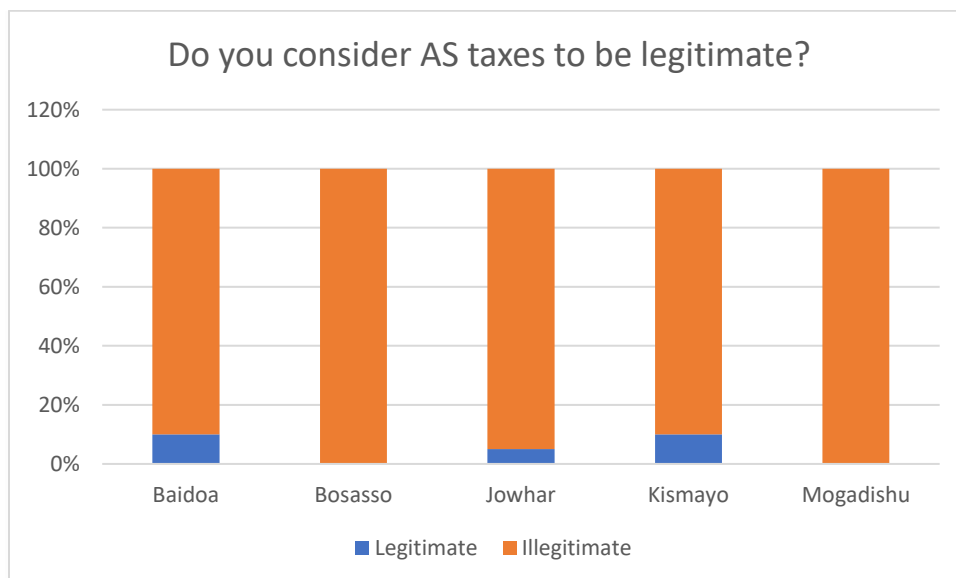


Figure 4 Percentage of businesses that consider AS taxes to be legitimate.³⁷

The government's response

AS's success in tax collection reflects the failures of the government to, firstly, enforce its existing regulations against the group's activities and, secondly, its failure to stop the group's

³⁷ This is based on fifteen taxpayers from each city.

infiltration of the government and get the information it needs to tax the business community. Of particular concern is the latter issue, which gives a sense of AS being an all-knowing entity, driving fear into the hearts of its foes and ensuring their compliance with its edicts.

The Somali government's response to the AS financial system is primarily the AML-CFT law and the regulations that are based on it. However, as we have seen, AS has not only succeeded in adapting to those measures, but it is also anticipating the government's next steps. Moreover, the implementation of some of the regulations are being hindered by the lack of a national ID system. This could have been useful in controlling the small-scale e-transfers, which are currently most of the payments at the checkpoints, and the way in which the group pays its members. Nevertheless, enacting a national ID system without implementing lessons learnt from the failing business registrations scheme will change little. New businesses would rather print a fake certificate than pay what they consider as unfairly high registration fees at both local and federal levels; because there is no verification system, they are able to conduct their businesses in this manner.³⁸ Therefore, any national ID system adopted by the government should be easily verifiable and not easily duplicated by an adversary.

The next step in the group's evolution in tax collection, and which the government is not controlling now, is e-money and money transfers to AS areas. Likewise, bank deposits and transfers are done without any supporting documents – an oversight that is not the financial institutions' fault, but the government's lack of imagination and failure to enact appropriate rules. Enacting regulations that make it harder for the group to move around money, pay salaries, and collect taxes using the financial system will hamper its ability to function in its current form. At the very least, implementing the recommendations in this paper will make it impossible for AS to pay its fighters, settle its debts, and obfuscate its dealings using its current methods.

The regulations alone will not have a major impact on AS finances without creating the necessary security environment to deny it the ability to threaten and punish tax resisters. Businesses and individuals are more likely to reject AS taxes in places where the security situation is more reliable, and the group is less able to conduct operations. Security is therefore a major issue in encouraging businesses to resist AS taxes. As we have seen, senior military commanders are being forced to pay AS; it is therefore neither practical nor reasonable to expect civilians to risk their lives in order to reject payments to AS.

³⁸ Businessman in Mogadishu, Oct 2020.

An important enabling factor in the AS tax collection is its ability to access the seaport manifest at will, through its government sources there.³⁹ Traders are therefore unable to hide the nature and volume of their imports from the group and, coupled with the group's operational capability in the urban areas, it is difficult for businesses to refuse to pay the group. By taxing in government areas and enforcing its edicts therein, it can undermine the legitimacy of the government and run its state within the state.

Conclusion

AS taxes are equal in value to, or more, than the FGS and FMSs in southern Somalia. It is the sole tax collector in the countryside, and this gives it access and influence that other Somali polities do not have. By keeping a record of the number of people and their wealth in the countryside, the group is able to achieve not only increased collection of taxes, but also gain a semblance of legitimacy, as tax payment is a sign of legitimacy. However, payment of taxes in the urban setting where the group is not in direct control is widely seen as illegitimate. The only taxpayers based in the cities that saw AS taxes as legitimate were cargo truck operators. This is because they received services in return for the taxes they paid to the group: security and safe passage in all areas controlled by the group. All the other businessmen considered AS taxes to be illegitimate.

The AML-CFT regulations are just currently being implemented, although AS has moved a few steps beyond it. Our recommendations in the policymakers' version are therefore meant to counter the current and anticipated countermeasures that AS will adopt as the AML-CFT comes into full force. Likewise, we recommend that appropriate grace period be given for businesses and financial institutions to implement these measures before they come into effect. Implementing these without a grace period will hurt businesses, as more than 50% of small businesses are run in the name of persons and not registered as businesses.⁴⁰ Enacting these recommendations will not only counter terrorist financing, but also increase the government's tax collection, as the AML-CFT is intended to do.

While it will obviously adapt to these measures, we expect the scale of its collection and financial distribution to be irreversibly damaged. It will rely more on physical cash collection,

³⁹ MP in the Parliamentary Finance Committee, Oct 2020, and MP in the Parliamentary Security Committee, Oct 2020.

⁴⁰ Senior bank official in Mogadishu, Sep 2020.

which will endanger its collectors and continue exposing its financial collection centers. Additionally, it will be slower in collecting, and even slower in paying its dues. With time, this will impact its operational capability and slow its momentum. Cases of individuals absconding with its monies will be more common and cause it to be severely cash-strapped in the long-term.